MALT BEVERAGE INTERBRAND COMPETITION ACT

HEARINGS

BEFORE THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

NINETY-SEVENTH CONGRESS

SECOND SESSION

ON

S. 1215

A BILL TO CLARIFY THE CIRCUMSTANCES UNDER WHICH TERRITORIAL PROVISIONS IN LICENSES TO DISTRIBUTE AND SELL TRADEMARKED MALT BEVERAGE PRODUCTS ARE LAWFUL UNDER THE ANTITRUST LAWS

JUNE 21 AND AUGUST 5, 1982

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MALT BEVERAGE INTERBRAND COMPETITION ACT

MONDAY, JUNE 21, 1982

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, D.C.

The committee met, pursuant to notice, at 9:35 a.m., in room 2228, Dirksen Senate Office Building, Senator Paul Laxalt (acting chairman of the committee) presiding.

Present: Senators Thurmond, Laxalt, Simpson, and Metzenbaum.

Staff present: Marcy J. K. Tiffany, chief economist and antitrust counsel; John F. Nash, Jr., chief counsel and staff director, Subcommittee on Regulatory Reform; and Boyd Hollingsworth, counsel to Senator Simpson.

OPENING STATEMENT OF SENATOR PAUL LAXALT

Senator LAXALT. The committee will come to order.

This morning the Senate Committee on the Judiciary will consider S. 1215, the Malt Beverage Interbrand Competition Act. The stated purpose of this act is to clarify the circumstances under which territorial provisions and licenses to distribute and sell trademark malt beverage products are unlawful under the antitrust laws.

The legislative initiative is sponsored by my friend and distinguished colleague from Wisconsin, Senator Proxmire. He has garnered broad support for the Malt Beverage Act in the Senate with 63 cosponsors. It is also widely supported by the malt beverage industry and its unions.

In the last Congress, we passed into law the Soft Drink Act. That was the legislation from which this legislation was patterned. At that time, the Federal Trade Commission asserted that the territorial arrangements in the soft drink industry constituted unreasonable restraints of trade. This was seen as a misapplication of the rule of reason to vertical territorial arrangements as required by the Supreme Court's decision in *GTE Sylvania*.

This committee's inquiry will focus on the guidance or the unworkability of our antitrust laws as they are currently applied to the malt beverage industry. I note that today's hearing includes a number of distinguished witnesses knowledgeable on this subject. On behalf of the committee, I might say that we look forward to their testimony.

The first witness we have is my colleague and very distinguished senior Senator of the State of Wisconsin, Senator Proxmire. Proceed in any fashion that you wish, Senator.

STATEMENT OF HON. WILLIAM PROXMIRE, A U.S. SENATOR FROM THE STATE OF WISCONSIN

Senator **Proxmire**. Thank you very much, Mr. Chairman. I appreciate this opportunity to testify before the committee in support of S. 1215, the Malt Beverage Interbrand Competition Act.

As you say, we now have 64 sponsors of this measure. I might say that many proposals currently abound to amend the U.S. Constitution for one purpose or another, and I support some of them. But today's hearing concerns a bill whose main purpose is to clarify an amendment that is already a part of the Constitution.

I refer, of course, to the 21st amendment, section 2 of which reads as follows: "The transportation or importation into any State, territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited."

This amendment grants power to the States to regulate the manufacture, distribution, sale, and consumption of malt beverages. But recent court decisions have raised doubts about the validity of State laws that either permit or require the three-tier, territorial system of distribution in the brewing industry.

At the very least, present litigation creates uncertainty about the continued viability of the three-tier, territorial malt beverage distribution system.

At worst, if the courts ultimately decide that this system—and the State laws governing it—violate Federal antitrust laws, then it seems clear that the participants in the distribution system would suffer economic harm before remedial legislation could be passed.

For this reason, it is vital that the Congress pass S. 1215 and pass it this year. This is the only effective way to remove the legal uncertainties surrounding the present distribution system.

The provisions of S. 1215 are narrow and precise. Section 2 of the bill provides that nothing in our Federal antitrust laws shall render unlawful written agreements between brewers and wholesalers which give the wholesaler the exclusive right to sell a particular brand of malt beverages within a specified territory, provided that, in the words of section 2, "such product is in substantial and effective competition with other malt beverage products within that defined geographic area."

It is important to note, too, what S. 1215 would not do. First, this bill would not change the current prohibitions against price-fixing, horizontal restraints of trade, and group boycotts, if such arrangements would otherwise be unlawful. Second, S. 1215 would not take away the right to recover treble damages for injuries resulting from exclusive territorial agreements that do not meet the bill's stipulated requirements. Third, S. 1215 would not require brewers or wholesalers to enter into territorial agreements. Rather, it states that if substantial and effective interbrand competition exists within a defined geographic area, then such agreements are not prohibited by Federal antitrust laws.

Finally—and this is most significant—section 7 of S. 1215 states that, "This act shall not invalidate or affect any provisions of the laws of any State." What does that mean? It means simply this: under the express language of S. 1215, the States would keep all of their existing power to regulate the distribution and sale of malt beverages.

As I have pointed out, the States derive this authority from the 21st amendment to our Constitution. S. 1215 makes clear that this authority should remain with the States, where it belongs.

It is helpful to keep in mind that malt beverages are not like the multitude of other products in our commercial system. At every stage they are tightly regulated and controlled. It is the States which do the regulating. They regulate malt beverages unlike almost any other product. They regulate the hours of sale—we just had a change in our State on that—the age at which people can buy the product, the location of sellers. So, this regulation is something which the States have practiced for a long time. It is peculiar to this particular industry. It does not apply to soft drinks or to other industries in anything like the same way.

Passage of S. 1215 would help preserve and protect the rights of the States to conduct this regulatory process as they see fit.

Mr. Chairman, I want to emphasize as strongly as I can this essential point: S. 1215 is States rights legislation in the best sense of the term. By enacting this legislation, we would be making it absolutely clear that the 21st amendment means what it says. It is the individual States which have the right to regulate malt beverages within their borders. Each State determines what is best for its jurisdiction in the regulation and control of this product. That is what the 21st amendment provides. S. 1215 serves to clarify that amendment and to lift the cloud that court litigation has placed upon it.

Congressional approval of this legislation would be consistent with action taken just 2 years ago. In 1980, the Congress passed and the President signed into law the Soft Drink Interbrand Competition Act. S. 1215 merely puts the brewing industry on the same footing as the soft drink industry.

In passing the soft drink bill, Congress confirmed that the interests of consumers are well served by promoting equitable and vigorous competition among different brands of beverages. Passage of S. 1215 would signal a similar affirmation in the case of malt beverages.

In addition, approval of S. 1215 would aid malt beverage wholesalers—and they include many small businesses—in their efforts to distribute their products in the most effective and economical way.

I urge that the committee act favorably on S. 1215 and report it out at the earliest possible time.

I might just say in conclusion, Mr. Chairman, that I am followed, I understand, a little later by a distinguished constituent, Frank Sellinger, who is the vice chairman, president, and chief executive officer of Joseph Schlitz Brewing Co. in Milwaukee, the beer that made Milwaukee famous. I might also say that I understand I am being followed immediately by a man I have great respect and admiration for, Fred Kahn, who I think served this country very well here in Washington. But even Fred Kahn is not perfect; even he makes mistakes. And this morning he is going to make one because I think he is going to oppose this bill. I say that because this kind of balances the weekend for Fred. You know, he was out at Northwestern University, and he received a doctorate of laws for his distinguished service to our country. He richly earned that. But I hope that you will listen to Fred with a degree of skepticism. He is a fine man but, as I say, he is fallible.

Senator LAXALT. I think the committee has been duly warned, Senator.

I notice that during the course of the Senator's testimony the esteemed chairman of the committee came in. Senator Thurmond, would you like to be heard now? I know that you have an otherwise busy schedule this morning.

The CHAIRMAN. Thank you very much, Mr. Chairman. I think we have got such an able chairman of this special committee hearing this matter, Senator Laxalt, that you can go right ahead with it. I have another appointment. I just wanted to come by for a few minutes. Thank you.

Senator LAXALT. I thank the chairman. Senator Metzenbaum?

OPENING STATEMENT OF SENATOR HOWARD METZENBAUM

Senator METZENBAUM. I am not going to be able to stay; however, I have a strong interest in this legislation. I have concerns about it. I hope that the witnesses will address themselves to the question of an additional antitrust exemption. It is no secret that, when the other measure came up which my distinguished colleague and good friend talked about—the matter of providing an exemption for the soft drink bottlers—I saw fit to oppose that legislation. It is also no secret that I did not provide such an overwhelmingly persuasive case that I got many of my colleagues to go along with me.

On the other hand, it is fair to point out that I think that a very effective and persuasive lobbying job was done by the soft drink bottlers. I am not sure whether I lost it on the merits or for political considerations. But those things do occur, and I am a realist enough to recognize it.

Be that as it may, I have some very strong feelings that antitrust, effective antitrust enforcement and implementation is the finest expression of the free enterprise system working and operating at its best. When free competitive forces have an opportunity to work, it adds to the viability of the capitalist system. I therefore have made it a policy almost with no exception to oppose exemptions from the antitrust laws and have done so on any number of occasions. I think, as far as this Senator is concerned, that the burden of proof is on those who would propose this legislation to convince the Members of the Congress that there is a special reason or a special need for an exemption from antitrust laws in this instance, and that without an exemption the industry cannot preserve its economic viability.

I also believe that there is a burden to prove that the consumers will not be hurt by eliminating the opportunity for free competitive forces to work. I have had a number of my own constituents speak with me on this subject. I have listened and listened attentively. I am sorry that I cannot remain to hear all of the testimony. But I know that this is a somewhat controversial piece of legislation, and I am very happy to hear the views of my distinguished colleague from Wisconsin with whom I probably am in agreement as much as with almost any Member of the Senate. Certainly, his testimony in support of this legislation is persuasive but whether it is compelling I am not quite certain at this moment. Thank you, Mr. Chairman.

Senator LAXALT. I thank the Senator. Senator Proxmire, I know that you have a busy morning as well. The opposition which the committee has received roughly followed these lines: The passage of the legislation would mean that the retailers would only have one source of supply for a particular brand of beer in a particular territory. Because of this monopoly, consumers would be at the mercy of that single distributer. What does the Senator have to say in response to this contention?

Senator PROXMIRE. What I would say in response to that is in the first place, of course, this bill does not require that you put this into place. What it does is to permit the States to determine whether or not it is, in their judgment, in the best interest of their State regulation and competition to have a single wholesaler provide the particular product.

But I would also say that the important element here is that there must be competition. I made that as clear as I could in my statement. There must be competition among brands. In other words, you are not going to have a single wholesaler as the only one who can make beer available. He may be the only one who can make Heileman or Schlitz or whatever available but not the only one who can make beer available at all in the area.

So, I think it does preserve competition, No. 1. No. 2, it leaves that regulatory decision to the States, where it belongs.

Senator LAXALT. The opposition contends—and I guess this is fairly essential to the whole problem—that the bill really creates a monopoly for one industry; it eliminates competition, which is the backbone of the free enterprise system. I think that is basically the concern which has been expressed here by Senator Metzenbaum. What is your answer to that contention?

Senator PROXMIRE. As I say, in the first place, there is nothing in the bill that mandates that you cannot have competition between wholesalers on the same brand. The bill says if a State wishes to confine that competition, it can do so. The essence of competition in our system is not necessarily a competition for exactly the same product; it may be a competition between or among products. All the advertising is aimed that way. What the customer is concerned about is having availability of choices so that he can take Pabst or Heileman or any other good Wisconsin beer.

Senator LAXALT. So, essentially, you are saying that what is granted here is an exemption and an exception to the Federal antitrust statutes, but nothing whatsoever would mandate any of the existing States under their laws to adopt this kind of legislation.

Senator PROXMIRE. Yes. And what this bill does, of course, is to simply follow the clear provisions of the 21st amendment, section 2 of which specifies that, "the transportation or importation into any State, territory, or possession of the United States for delivery or use therein of intoxicating liquors in violation of the laws thereof is hereby prohibited." It simply says that it is up to the State to decide. We put that into the Constitution. What this bill does is to simply clarify that.

Senator **Laxalt**. Tell me this then, Senator. Haven't some of the States rejected this approach on a State level?

Senator **Proxmire**. Pardon me?

Senator **Laxalt**. Some of the States have rejected this kind of legislation purely on the State level.

Senator **Proxmire**. Certainly.

Senator **Laxalt**. The somewhat haphazard condition of case law has resulted in the introduction of such legislation. In reviewing the situation, one must examine the potential impact on a State which neglects to enact such legislation.

Senator **Proxmire**. Then there is no question. Any wholesaler who wanted to come in and have an opportunity to sell the same product in the same territory would have a perfect right to do so and could not be prohibited if the State permitted it. It would be up to the State.

I think the chairman has put his finger on the exact significance here. We are giving the State the opportunity to make the decision on regulation in strict accordance with this provision of the Constitution, the 21st amendment.

Senator **Laxalt**. In the absence of this legislation, what is the situation?

Senator **Proxmire**. In the absence of the legislation, as I indicated, at best you have a situation of confusion. At worst, quoting from my earlier testimony, "if the courts ultimately decide that this system—and the State laws governing it—violate Federal antitrust laws, then it seems clear that the participants in the distribution system would suffer economic harm before remedial legislation could be passed."

It takes us months, sometimes years to act. Meanwhile, a number of companies and their employees would suffer a serious economic damage.

Senator **Laxalt**. I thank the Senator. Senator Thurmond, do you have any questions?

The Chairman. No, Senator.

Senator **Laxalt**. Senator Metzenbaum?

Senator **Metzenbaum**. No questions, thank you.

Senator **Laxalt**. Thank you very much, Senator Proxmire.

Senator **Proxmire**. Thank you.

Senator **Laxalt**. You have been very helpful.

We will now hear from Prof. Alfred Kahn, the National Institute of Economics and Law, Washington, D.C. Welcome. It is nice to have you back.

Unfortunately, Senator Robert Kasten could not be here today due to the existence of a previous engagement. However, he has prepared a statement of his support for S. 1215 and requests it be included in the record. Without objection, it will be included along with the text of the bill.

[Prepared statement of Senator Kasten and S. 1215 follow:]

PREPARED STATEMENT OF SENATOR ROBERT KASTEN BEFORE THE SENATE JUDICIARY COMMITTEE IN SUPPORT OF S. 1215, THE MALT BEVERAGE INTERBRAND COMPETITION ACT

Mr. Chairman, I am very pleased to be able to place in the record today this statement in support of Senate bill 1215, the Malt Beverage Interbrand Competition Act. Enactment of this legislation will strengthen the system by which beer and other malt products are distributed by promoting fair and vigorous interbrand competition through stimulation of wholesalers' efforts to distribute malt beverages.

Mr. Chairman, I believe this legislation is especially important to the many small beer wholesalers in this country. Passage of this bill will allow small businessmen who desire to go into the wholesale business to establish and build up their businesses without fear that other wholesalers selling the same brand of beverage will prevent them from getting started. A prospective wholesaler will be more willing to make the capital investment needed to begin business if he knows his sales territory is secure. Under this provision small wholesalers already in business can build up their territories to compete more effectively with wholesalers of other brands of beer when territorial rights to their own brand is secure.

This bill extends to the brewing industry the same rights and opportunities that the soft drink industry has already been afforded. As in the soft drink industry this legislation creates opportunities, not regulations or requirements. The bill simply makes clear that brewers and wholesales are not prohibited by the Federal antitrust laws from electing to enter into agreements that would strengthen their interbrand competitive efforts.

The actual provisions of S. 1215 are not mandatory. They allow brewers and wholesalers to enter into written agreements granting the wholesaler an exclusive right to sell a particular brand of malt beverage within a particular territory, provided the beverage to be sold is in substantial and effective competition with other malt beverages in the area. The bill thus provides an exclusion from Federal antitrust law only in this narrow area.

A State is not precluded by this legislation from regulating the malt beverage industry within its borders. By simply providing an exclusion from Federal antiturst laws, this bill returns the regulation of the malt beverage industry to the States, which is where it rightfully belongs.

Mr. Chairman, the legislation before us does not affect other provisions presently in the law that protect the interests of consumers. Prohibitions against pricefixing and restraints of trade are not changed by this bill, and remain in full force and effect.

S. 1215 has widespread support from both brewers and wholesales in the beer industry. It is also supported by labor unions involved in the brewing industry. In addition, Mr. Chairman, this legislation has widespread bipartisan support here in the Senate, with 63 of our colleagues signed on as conspONSORS. The companion bill in the House enjoys equally strong support.

In conclusion, Mr. Chairman, I believe this is a good bill. It will strengthen our malt beverage industry by providing security to wholesalers and at the same time will promote vigorous interbrand competition among the various brands of malt beverage on the market. It will leave regulation in this narrow area to the individual States where it rightfully belongs and at the same time will leave other Federal safeguards intact. It will cost the Federal Government nothing and will thus not impact the budget. Mr. Chairman, the malt beverage industry, and small businessmen within the industry in particular, need quick action on this legislation.

Mr. Chairman, thank you very much for your attention to this matter.

97TH CONGRESS
1ST SESSION

S. 1215

To clarify the circumstances under which territorial provisions in licenses to distribute and sell trademarked malt beverage products are lawful under the antitrust laws.

IN THE SENATE OF THE UNITED STATES

MAY 18 (legislative day, APRIL 27), 1981

Mr. PROXMIRE (for himself and Mr. KASTEN) introduced the following bill; which was read twice and referred to the Committee on the Judiciary

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A BILL

To clarify the circumstances under which territorial provisions in licenses to distribute and sell trademarked malt beverage products are lawful under the antitrust laws.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. This Act may be cited as the "Malt Beverage Interbrand Competition Act".

SEC. 2. Nothing contained in any antitrust law shall render unlawful the inclusion and enforcement in any written contract entered into after the effective date of this Act by any brewer, importer, trademark owner, or trademark licensee of a trademarked malt beverage with any wholesale distributor of provisions granting the wholesale distributor the sole and exclusive right to distribute and to sell such product in any defined geographic area within any State and limiting such exclusive distributor to the distribution and sale, directly or indirectly, of such product only for ultimate resale to consumers within that defined geographic area when such product is in substantial and effective competition with other malt beverage products within that defined geographic area.

SEC. 3. Nothing in this Act shall be construed to legalize the enforcement of provisions described in section 2 of this Act in any written contract described in that section by means of price-fixing agreements, horizontal restraints of trade, or group boycotts, if such agreement, restraints, or boycotts would otherwise be unlawful.

SEC. 4. As used in this Act the term "antitrust law" means the Act entitled "An Act to protect trade and commerce against unlawful restraints and monopolies" (Sherman Act), approved July 2, 1980, the Federal Trade Commission Act, approved September 26, 1914, and the Act entitled "An Act to supplement existing laws against unlawful restraints and monopolies, and for other purposes" (Clayton Act), approved October 15, 1914, and all amendments to such Acts.

SEC. 5. As used in this Act "malt beverage" shall mean and include beer of all types and varieties as defined in any

Federal or State statute, ale, porter, stout, and all other similarly designated fermented beverages containing one-half of 1 per centum or more alcohol by volume.

SEC. 6. As used in this Act the term "State" includes the District of Columbia and any territory or possession of the United States.

SEC. 7. This Act shall not invalidate or affect any provision of the laws of any State.

STATEMENT OF ALFRED KAHN, NATIONAL INSTITUTE OF ECONOMICS AND LAW, WASHINGTON, D.C.

Mr. KAHN. Thank you, Mr. Chairman. I will not waste any more of my 15 minutes with courtesies.

Senator METZENBAUM. Mr. Kahn, would you tell us at the inception on whose behalf you are testifying? Also, who is the National Institute of Economics and Law, which I probably should know but I do not?

Mr. KAHN. It is a newly formed public interest economic research group on whose board of advisers I sit. Of course, I was going to observe immediately that my testimony is sponsored by this national institute.

It has undertaken an analysis of these bills, but it has done so with support from the Food Marketing Institute. I would like you to know that as well.

I am afraid I will have to return Senator Proxmire's kind words. He, too, rarely makes a mistake but, like Fiorello LaGuardia, when he makes one it's a beaut.

I apologize for my inability on this short notice to present written testimony, but we will submit for the record a report that was prepared by the national institute on this bill. I served as adviser to the institute on that report, and I agree with it in all its essential respects.

Incidentally, I want to point out also that I am not an expert on the beer industry. For that reason I have asked Dr. Michael Kavanaugh, who is research director of the institute, to sit next to me so that, if there are questions in detail about the research he has done, he can help us answer. Is that permissible?

Senator LAXALT. Surely.

Mr. KAHN. Finally, I want to observe that I am not an expert on the beer industry, but I have taught and written extensively on the antitrust laws. I served on the two major Federal commissions studying the antitrust laws under Presidents Eisenhower and Carter. I have done a great deal of work on the distribution of soft drinks. I tried to get President Carter to veto the soft drink bill, one of my less-than-glowing successes in my job as inflation czar, a title that I did not coin.

I would like to begin with a couple of words about the general practice that we are witnessing here, which I think is becoming increasingly prevalent, to which Senator Metzenbaum alluded, the practice of individuals, of companies and industries before, after, during the course of antitrust proceedings to turn to Congress for special legislation to exempt them. I made a point of inquiring about this legislation whether on its face it merely exempts people from liability in the cases where States require such exclusive territorial distribution, and the language of the bill does not say that. The bill provides a blanket exemption from the antitrust laws for all such agreements between brewers and distributors regardless of State action. I think it is quite important that you look into that because I believe it is not, therefore, simply a question of giving Federal permission to the States for their actions.

I think there is obviously no impropriety in people turning to Congress for special legislation of this kind. But I do urge you to show very great restraint about interfering with the normal process of the enforcement of the antitrust laws in this ad hoc manner. The antitrust laws are only laws, but, as has been observed many times, they have a generality, a fundamental characteristic that is very similar to provisions in the Constitution.

There is a great body of precedent. The law has shown great capacity for flexibility in its interpretation and in particular the development of a rule of reason, particularly with respect to exclusive territorial franchises, to evaluate under the rule of reason the arguments that will be posed for and against the practice.

So, I respectfully urge you—excuse me, sir.

Senator LAXALT. I was just going to say before you go to your next point, Professor, would you amplify, for the purpose of the record and the edification of my colleagues who are not present, what the rule of reason is all about?

Mr. KAHN. I think I should begin with its opposite. Under the antitrust laws, there are certain practices which are per se illegal, without any further inquiry into the presence of power or into their consequences. Price fixing is one of those. There are others in which, while there is a restriction on competition involved, such as there clearly is when you say you have an exclusive arrangement which excludes other people in a particular market from distributing your products, but there may be compensating advantages from the point of view of invigorating competition. In such circumstances where the law holds that the practice is not unequivocally bad and therefore to be outlawed per se, it is incumbent on the courts and the antitrust agencies to weigh the restrictive effects against the possible benefits.

That is the nature of the rule of reason. That is a very general statement. I think perhaps for present purposes it suffices.

Senator LAXALT. Thank you.

Mr. KAHN. Again, I respectfully suggest that Congress, having set up the law and the process, should exercise great restraint in interfering, in short-circuiting the process, and place on the proponents of such special interest legislation a very heavy burden of proof that the ordinary procedures will involve extraordinary hardship and injury to the public.

My second point is this: I think it absolutely beyond argument that exclusive territorial franchises do restrict competition in a very serious number of ways. The essence of competition, the essence of a free enterprise system is freedom of entry. When we deregulated the airlines and the trucking industry, the first thing we did was to say anybody who wants to enter this industry may. Exclusive territorial franchises restrict freedom of entry into the market.

Who are the most likely entrants into any market for distribution of soft drinks or beer? They are the ones who, by virtue of the possibility of their entry, exert the most effective competitive discipline on people in the market. Clearly, they are the people who are already in the same line of business in adjacent markets. And notice it is just like airlines. The ones who are most likely to come in to a particular market if service is bad, the ones who are most likely to come in if prices are too high are the people in adjacent markets. It is exactly that kind of entry that exclusive territorial franchises prevent.

Why would buyers ordinarily turn to people in adjacent markets? The main reason would be to get a better price. We found in soft drinks that there is as much as 30 to 40 percent difference in prices in the same marketing territory between one franchise territory and another. If markets were free, this would give buyers the opportunity to play one supplier of a particular product off against another. So, the main kind of competition that exclusive territorial franchises would weaken would be to suppress the possibility of that kind of price competition, bargaining with people in adjacent markets to see if you could get a better price.

This also has inevitable undesirable effects on efficiency. There is no more powerful force pressing people constantly to be more efficient than the pressure of price competition. Again, we have discovered that in airlines in the last 2 years.

Exclusive franchises also place arbitrary geographic limits on the ability of firms to grow, often small businesses who can best grow by going into adjacent markets and achieve the economies of scale.

Finally, the more concentrated the supply industry is the more likely you are going to get a discouragement of price competition under this practice at the local level. If you can have only one distributor for each brewer at the local level, then you, in effect, transfer the concentration at the national level right down to the local market. If, as in beer, you have high concentration—in 1981 the top two brewers accounted for 52 percent, just two, of the national market; the top six accounted for 82 percent of the national sales—then that means that you are going to have that high concentration at the local level if you can have only one representative for each manufacturer or brewer.

Moreover, the local concentration will ordinarily on the average be higher than that, for two reasons. First, not every national brewer is represented in every local market. Second, there is a widespread practice of distributors handling the products of more than one brewer.

In the institute's report there is a survey from some 25 representative cities, which shows that for the typical case as many as one-third to two-thirds of the distributors handle more than one product—not just more than one brand but the product of more than one brewer. So, you have high concentration ratios at the local distribution level if you cannot have intrabrand competition—that is competition between different distributors of the same brand.

The report is able to marshal only anecdotal evidence of the effect that this has on price. It explains why it is very hard to do comprehensive statistical comparisons. But it does cite the case of Indiana, which in 1974 abolished exclusive territorial franchises. According to reports in the trade, prices dropped 20 percent.

I have done rather extensive studies in the soft drinks area. There it seems clear that prices have—both the proponents and the opponents of exclusive franchises concede—the ones concede; the others agree—that it has prevented some kinds of price competition and held prices up.

The third point—I believe I will make my time constraint—there may, of course, be offsetting benefits. The defenders of exclusive franchises assert that it can lead to more effective competition between brands. That is why we have a rule of reason, to examine the possible beneficial effects. But it is very important that you not fall into the trap of many observers in this field of assuming that it is a simple question of these franchises discouraging intrabrand competition but clearly encouraging and strengthening competition between brands. That is not true.

It is important to recognize that exclusive franchises also interfere with competition between brands. If a Miller's distributor in Baltimore cannot come into Washington and distribute because there is an exclusive Washington distributor of Miller's, then that Baltimore distributor of Miller's is prevented from competing not only with Miller's in Washington but also with Anheuser Busch and with Pabst and the other people. In short, by preventing any interpenetration by a second distributor of a particular brand, it prevents and discourages competition with all brands, not just within the individual brand.

Also, it tends to divert competition to service and to advertising. In fact, that is one of the arguments in favor of it. But I would contend that often advertising competition is far less valuable to the public than price competition. And that is the kind of competition that this bill would weaken.

Finally, you will, of course, want to weigh the arguments that in some ways at least these exclusive franchises do permit or do lead to invigorated competition among brewers, interbrand competition.

I think the proper general principle for you to apply is to ask, is limiting intrabrewer competition necessary to achieve these ends? Are there other ways available that will be less restrictive of competition? Is this the most efficient way of achieving those ends? And, in the end, do the benefits exceed the costs?

I am very skeptical that the beer case can stand up against those questions.

One of the main ways it is argued in beer you have to have exclusive franchises is the so-called free rider problem. If one distributor advertises in a territory, if there is more than one distributor of that brand, he will be discouraged from advertising because the sales will go to somebody who does not advertise but who sells the same brand. But there is no such problem with advertising by the brewers. The brewers have every incentive to advertise, and that is where most of the advertising evidently takes place. Philip Morris is the fourth biggest advertiser of all companies in this entire country. Anheuser Busch is the 21st biggest advertiser. Moreover, there is no such problem if retailers advertise because they know that, if they advertise, they will have the name of their store on it and they will get the business.

There is no problem with joint advertising between distributors and retailers such as we have all the time, in which the distributors will give them a special price and then they will put a big ad in Thursday's newspapers. There again, the benefit will go to the advertising retailer.

So, the only advertising that may be discouraged is general advertising by the distributor. That, I suggest, is very unimportant from the point of view of the public welfare.

There is a final argument, which will be my last, and that is about stale beer. Beer does get stale, I am told; I have never discovered it, but I am told. The contention is that, only if one distributor has total responsibility for sales in the territory, will it have a total incentive and responsibility to see to it that stale beer is taken off the shelves before it can be sold. This argument has some plausibility.

Clearly, however, the brewer also has a strong incentive to see to it that people do not buy his beer and it is stale. The retailer has a strong incentive that people not buy his beer and it is stale. The customer has a strong incentive not to buy stale beer.

Senator LAXALT. I would like to comment on that point which presupposes that the States and locals would permit this condition to continue. Would not the States and locals have an interest in keeping stale beer off the shelves as much as the Feds if not more so?

Mr. KAHN. Of course they would. But, if you leave it to a market in which you do not permit exclusive territorial franchises, then the question——

Senator LAXALT. There will be less discipline. Is that what you are saying?

Mr. KAHN. Yes, there is less discipline because one distributor may say: Well, it's not my beer; it's somebody else's beer. Whereas, if he is the only one in the territory, then it is clearly his beer.

But what I am saying is that, even if the State does not do anything, even if the distributor does not, the brewer is going to want to see to it that his beer is not sold when it is stale. The retailer is going to want to see to it, and the customer. So, you can easily then handle it by the retailer policing the shelves. As I understand it, most beer or all beer has coded dates on it. So, a retailer can tell if it is stale. If the brewer is worried, the brewer can put dates on it just as in the case of milk and say don't buy this after a certain date.

Again, I do not think you have to have a restriction on competition in order to do it. So, even in this one last plausible case it seems to be highly likely that it will fall if you ask searching questions of the advocates: How important is the problem, is exclusive franchising the most efficient way of handling it, the least restrictive way, or are there other better ways. And these are exactly the kinds of questions that the courts would apply under the rule of reason.

That brings me back to my first point. I urge you to place on proponents of these bills a very heavy burden of proof that your stepping in to help the special industry and give it a preferential exemption from the normal processes of the antitrust laws is necessary in the interest of the public. Thank you very much.

Senator LAXALT. Thank you very much, Professor Kahn. Have no fear concerning the burden of proof point. In the last couple of years, this committee has been besieged—I think that is the proper term—on the part of interested groups wanting out from under antitrust.

Mr. KAHN. Exactly.

Senator LAXALT. It is all the way from the NFL to several other groups. I think the sensitivity of the committee in this respect is very high at this point. We will certainly insist that the proponents of this legislation maintain a heavy burden of proof.

Professor Kahn, I am going to have to be somewhat limited in my questions because the panel here is extensive.

Do you disagree with Senator Proxmire's basic premise that the net effect of this legislation does not mandate to the individual States that they do anything about the problem, but simply gives them the authority to do so if they wish?

Mr. KAHN. Well, I am not an expert on this particular law or the intent of the committee. The language says that the antitrust laws shall not apply to agreements between brewers and distributors conferring on the latter exclusive franchises. It does not say they shall not apply only in those cases in which it is legalized by the States. So, to accomplish Senator Proxmire's purpose, which I am not sure I would advocate either——

Senator LAXALT. It is my understanding, that there would be rampant confusion and all the other attendant problems, Professor. We can do whatever we want here, but nothing happens unless a State would implement this legislation.

Mr. KAHN. That is not, as I understand it, what the legislation says. It says——

Senator LAXALT. Well, we had better look into it. That is certainly Senator Proxmire's contention, and I think the understanding of at least some of the members of the committee.

Mr. KAHN. I urge you to look into that.

Senator LAXALT. That is terribly important.

Mr. KAHN. Of course. And, of course, you remember——

Senator LAXALT. The points you raise are appropriate for consideration, all revolving around the rule of reason; certainly they would be points that could be raised in the individual State legislatures indicating why, in terms of their local conditions, they should not be granting this kind of preference.

Mr. KAHN. I agree.

Do remember, sir, that the 21st amendment was passed almost 50 years ago. I am a little bit surprised, the contention is that we have been living for 50 years in a state of schizophrenic confusion.

Senator LAXALT. That might be open to some discussion.

Mr. KAHN. Well, that is another story.

Senator LAXALT. I do not have any more questions, Professor. I thank you very much for coming in. As I say, in all probability we will be addressing some other inquiries to you——

Mr. KAHN. Please do.

Senator LAXALT [continuing]. Particularly on this jurisdictional point.

[The following material was subsequently supplied for the record:]

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Exclusive Territorial Distributorships and Consumer Welfare: The Case of Beer

Prepared by the

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Acknowledgement

This research report focuses on the inequities and inefficiencies of restricting entry in beer distribution markets. The report was prepared by Dr. Michael Kavanaugh, the research director of the National Institute of Economics and Law. Alfred Kahn, Professor of Economics, Cornell University, provided the author with extensive advice and adopted the report as the basis of his testimony before the Senate Committee on the Judiciary on June 21, 1982. Also contributing to the report were Robert M. Wolcott, Thomas Lamothe, Elizabeth Watson and Todd Berman. The editorial work was performed by Marilyn E. Matthews and Vernon W. Palmer, II.

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Summary

Presently pending legislation before the U.S. Congress (S. 1215 and H.R. 3269) would permit exclusive territorial franchises for distributors of beer to be established. This legislation, it is argued, will improve product and service quality, correct inequities in the allocation of costs among distributors and aid small business in its quest for survival. A review of the present conditions of competition and performance in wholesale beer markets and an analysis of the merits of granting exclusive franchises suggest the following conclusions:

- There is no evidence to indicate that either retail or wholesale markets for beer in the U.S. are failing to function effectively.
- Exclusive territorial distributorships will reduce the ability of new firms to enter the beer distribution market and thereby reduce consumer welfare.
- Exclusive territorial distributorships would reduce price competition thereby increasing beer prices.
- Exclusive territories would facilitate a redistribution of purchasing power from consumers of beer to brewers of beer.
- Exclusive territories would reduce the incentives to innovate in distribution technologies thus retarding efforts to reduce unit costs.
- There is no significant evidence that product quality, i.e., stale beer, is currently a problem and further there is no reason to conclude that allowing exclusive territories is

the least cost approach to remedying such a problem. The use of open dating appears to be the least cost and most efficient mechanism for maintaining the quality of beer sold.

- There is no empirical evidence to indicate that a substantial free riding problem, i.e., the sales of beer by some distributors at the advertising expense of others, exists. The most efficient form of correcting such a problem, should it ever develop, is more effective advertising.
- Due to the lack of any systematic relationship between firm size and beer sales, it is not evident that the granting of exclusive territories will advance the objective of enhancing the economic health of small business.

The legislative proposal to allow exclusive territories is premised upon the assertion that market failure is occuring in the beer industry. We have found no evidence of such failure. In the event that market failure was present, the granting of exclusive territories would have to be shown to be the most effective and the most efficient means of correcting the failure as well as that policy which yielded maximum net benefits. On all these criteria, exclusive territories appears to be an inferior policy, both technically and socially.

I. Introduction

This report sets out the likely consequences for consumer welfare of permitting manufacturers (brewers) of malt beverages (beer) to grant exclusive territorial franchises to distributors of beer.[1] The focus is on the general concept of exclusive territories for beer distributors and how their use affects prices, efficiency, innovation and service quality, rather than on any single piece of legislation.[2]

Some proponents of exclusive territories admit that higher consumer prices result, but instead claim that service quality is enhanced and that small business is protected (Posner 1977, p. 4.)[3] Second, they argue that inter-brand competition is strong enough to prevent the monopoly overcharges that might otherwise result from exclusive territories. Implicit in this argument is the assumption that there is no other means of achieving improved service quality or protecting small business that poses less of a risk to competition or is more efficient. These conditions are examined below.

Opponents claim exclusive territories give rise to overcharges, foster inefficiency, facilitate collusion and, in general, impair consumer welfare.[4] Further, small volume retailers bear the brunt of the overcharges and, more often than not, small volume retailers are small businesses. These issues are more fully examined below.

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[1] A distinction is drawn between exclusive dealers and exclusive territories. In the former, the dealer vends the product of one brewer, but need not confine the distribution to a specified area. In the latter, the distributor may vend the product of many brewers, but is confined to specified areas. It is possible for exclusive dealers to operate in exclusive territories.

[2] The 97th Congress saw the introduction of at least two pieces of legislation (H.R.3269 and S.1215) that would exempt brewers from antitrust law in awarding exclusive territories.

[3] Among the supporters of the legislation before the 97th Congress were the National Beer Wholesalers Association and the U.S. Brewers Association.

The plan of this report is as follows. Section II sets out the standards for judging the effects of exclusive territorial distributorships on consumer welfare. Section III deals with the effects of exclusive distributorships on prices, efficiency, innovation and service quality. Section IV treats the contribution of exclusive territories toward furthering the social goals of promoting small business.

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[4] Associations opposed to the legislation before the 97th Congress included the National Licensed Beverage Association, Congress Watch, Consumers Union, Consumer Federation of America, the U.S. Department of Justice and the Food Marketing Institute.

II. Consumer Welfare and Exclusive Territorial Distributorships

A. Consumer Welfare and Open Markets.

Consumer welfare is a multifaceted concept encompassing not only the level of purchasing power, but also its distribution among consumers. There is no generally accepted quantitative estimate of it. There are, however, standards whose achievement would ensure that society will be better off. Consumer welfare is advanced:

- when production is carried out in the least cost manner (no wasting of resources);
- when consumer prices reflect the costs of production, where costs of production are understood to include a normal rate of profit.[5]

Economists have long argued that "perfectly competitive" markets achieve the welfare standards and, therefore, advance consumer welfare. It has also been long argued that perfect competition--with its requirements for a large number of buyers and sellers, standardized, homogenized products and well-informed traders--is too stringent a criteria for policymaking.

Perfect competition, however, is not needed to achieve advances in consumer welfare. Contestable (open) markets also achieve the welfare standards set out above (Baumol, 1982). A contestable market requires that an entrant be able to compete with the incumbent, [i.e., suffer no disadvantage in production technique, face trivial sunk costs and operate in markets in which prices do not change instantaneously (Dixit, 1982)].

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[5] The differences in accounting conventions in American industry--and in owner-operated businesses--the failure to distinguish between returns to equity, risk-taking and owner-supplied labor prevent the translation of the concept of normal profit into a simple number. Normal profits may be observed in unregulated markets that exhibit no production or consumption externalities when there is no increase or decrease in the number of establishments. (See Section II-B for another qualification).

Looking at the beer industry, markets in which beer is distributed advance consumer welfare so long as there is potential for new distributors to enter the market easily. Entry may occur from the expansion of an existing distributorship or the formation of a new company.

To see that contestable markets achieve the same welfare standards as perfectly competitive markets, consider the adjustments if the standards are not met. First, if one beer distributor decides to charge higher prices to retailers, above normal profits are earned for a time. As long as markets are contestable, another distributor can enter the market and serve the retailer. In order to persuade the retailer to switch from the old distributor, the new distributor need only offer the retailer the old price. The incumbent distributor would either lose business or cease overcharging.

Contestable markets insure efficient production. If distributors are pricing their services so as to reflect the costs of production, but one distributor owns or leases too much warehouse space, that distributor's costs will be higher than another distributor's costs. The inefficient distributor will charge retailers higher prices than will an efficient distributor. The result is that the inefficient distributor loses business and the efficient distributor expands.

Innovation is strengthened by contestable markets. This is especially so in the case of contestable markets with price sensitive consumers. Innovations bring about reductions in unit costs. Reductions in costs enable the successful innovator to reduce prices and still earn normal profits. This reduction in price is a signal to retailers to increase their purchases from innovating distributors. Given price sensitive consumers, the increase in sales volume for the innovator represents an increase in total profits.

B. Consumer Welfare and Closed Markets

Exclusive territories reduce (perhaps eliminate) the ability of entrants to challenge incumbents in the marketplace. In effect exclusive territories, by erecting a barrier to entry, close markets. This reduction in the contestability of a market permits prices to be charged that are in excess of the costs of production. Furthermore, there is a reduced incentive to produce services as efficiently as possible and a reduced incentive to innovate. In short, the standards consistent with advances in consumer welfare are not met in markets that are closed.

C. Market Failure

Open markets sometimes fail to allocate resources to the highest and best uses. When failure occurs, achieving the welfare standard of pricing to cover the costs of production does not advance consumer welfare. It is important, then, to determine if the markets in which beer is distributed are examples of failed markets. If they are, then, exclusive territories might be necessary to remedy a market defect.

The relevant type of market failure when considering beer distribution may be termed a free-rider problem.[6] In this instance, a producer is able to avoid paying all of the costs of production by imposing some of the costs on third parties. For example, if one distributorship (the entrant) can force another distributor (the incumbent) to pay for advertising or monitoring product quality, then, the entrant can charge lower prices than the incumbent. The low price is bought, however, at the expense of the incumbent and perhaps at the expense of product quality. The extent to which an entrant into a beer distribution market is able to avoid paying all of the costs of production is minimal as will be developed in Section III-C, below.

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[6] Other types of market failure may be termed the provision of public goods and extreme scale economies. Beer distribution, obviously, is not a public good and there is no evidence that the distribution of beer is subject to strong economies of scale. See Section III-C below.

If it can be shown that the distribution of beer is plagued by free-riding problems, then the next question is what to do about it. The method of correcting a market failure may be judged by the following criteria:

- o the method is efficacious;
- o the method is efficient (it causes the least distortions to the functioning of markets); and
- o the method is beneficial (the distortions in market mechanisms caused by preventing free-riding do not impose costs--overcharges, inefficiencies, reduced innovation--that exceed the benefits of preventing free-riding).

Applied to exclusive territories, it must be shown that:

- o a free-rider problem exists;
- o exclusive territories will correct the problem;
- o exclusive territories are an efficient way to correct the problem;
- o when the free-rider problem is corrected, consumers receive sufficient benefit so that any costs of exclusive territorial distributorships are offset.

As will be shown below, none of these criteria can be met in the beer industry.

D. Conclusions

There need not be perfect competition in beer distribution for consumer welfare to be advanced as long as entrepreneurs are allowed to enter a market. Exclusive territorial distributorships reduce the ability of entrepreneurs to enter a market. Of particular importance is the effective discipline of potential entry provided by businesses operating in adjacent markets. This type of entry--which is far from hypothetical since natural market territories overlap--is artifically prevented by exclusive territories. Reduced entry opportunities raise consumer prices and blunt innovation. Hence, exclusive territorial distributorships impair advances in consumer welfare. It might still be possible for exclusive territories to advance consumer welfare, if there were a free-rider problem in the distribution of beer, and if exclusive territories would correct the free-rider problem in an efficient and beneficial way. Otherwise, exclusive territories must be found to be inimical to the interest of consumers.

III. Pricing, Efficiency, Innovation and Service Quality

A. Introduction

The 21st Amendment repealing prohibition delegated to the states considerable authority to regulate the production, distribution and consumption of alcoholic beverages.[7] Most states mandate that beer distributors be separate and independent of brewers, and that retailers deal only with distributors, not with brewers. This is the so-called 3-tier system. Not only do states mandate a middleman, but some states require that wholesalers have exclusive territorial distributorhips (Table 1). This prohibition against distribution outside of designated territories, whether authorized by state law or not, may be challenged under federal antitrust law. It is this litigation risk that recently proposed legislation (H.R. 3269 and S. 1215) would remove.

Other relevant regulations and laws include state taxation of beer, stipulations concerning the type of containers, size of containers, deposits on containers, location of advertising, alcoholic content, price posting laws and by requiring licenses for distributors and retailers. States also regulate retail sales by stipulating minimum ages, hours of sale and place of sale.

In addition to the regulation of alcoholic beverages, per se, states also regulate the general business environment. In particular, several states have franchise laws governing the relation, in this instance, between brewer and distributor. These laws limit the ability of brewers to end, unilaterally, a beer distributorship.

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[7] This review should not be construed to be an exhaustive presentation of the regulations governing alcoholic beverages.

Table 1

States that Prohibit Distributors to Sell Outside of a Designated Territory

Arkansas	Maryland
Colorado	Nebraska
Connecticut	Ohio
Georgia	Pennsylvania
Idaho[a]	Tennessee
Illinois	Utah
Kansas	Vermont
Maine	Virginia
	West Virginia

Source: FTC, Staff Report, The Brewing Industry, December 1978.

[a] Permits more than one distributor per territory.

The variations in regulation among the states provide opportunities and create difficulties for studying the effects of exclusive territories on consumer welfare. Since some states require exclusive territories while other do not, variations in prices, efficiency, innovation and service quality might be observed by simple comparison. The differences in state regulation, however, extend beyond exclusive franchising to taxation, point-of-sale requirements and the like. These other differences obscure comparisons. Furthermore, there may be *de facto* exclusive territories in states that do not prohibit distributors from selling outside of designated territories. Regardless of whether these "gentlemen's agreements" are in violation of the law, price, efficiency, innovation and service quality are affected with the obvious result of obscuring comparisons.

Another approach is to search for a state that at one time had exclusive franchising laws and then repealed the law. By adopting a before/after approach, differences in consumer welfare may be able to be quantified. Indiana is such a state and it provides a readily available case study of the effects of exclusive territories on consumer welfare.

Data, more often than not, are aggregated to the state or national level, but the market for beer is local. This tends to obfuscate important local relationships.

All in all, quantitative assessment of the effects of exclusive territories on consumer welfare is difficult but not impossible. Where quantitative comparisons are not possible, judgments may be made based on economic principles and on observation.

B. Pricing

1. Competition

A policy change may help or hinder the setting of prices close to the costs of production. Prices that are close to the costs of production are good for the consumer and mean that the purchasing power needed to obtain a good is about equal to the value of the resources needed to produce the good. Open markets promote this end and the phenomena may be termed price competition.[8],[9] Price competition may be indicated by the responsiveness of one competitor's sales to another competitor's price change. For example, if the price of an Anheuser-Busch (A-B) product is decreased and sales of a Miller product decrease, it may be said that there exists price competition between Miller and A-B. Continuing, if the price of an A-B product decreases and the sales of Miller do not decrease, it may be said that consumers are loyal to Miller and price competition between A-B and Miller is slight.

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[8] There is a pattern of prices within any one beer market reflecting consumer perceptions of different categories or grades of beer, premium and popular, for example. There are, however, no important differences in the cost of labor or materials for the various grades of beer (Elzinga, 1971).

[9] In recent years the retail price of beer consumed in the home increased more slowly than the rate of inflation. This happy result says nothing about the desirability or undesirability of exclusive territories. The explanation may be found by noting that 15 to 20% of the ingredients used to make beer are agricultural products whose prices did not rise as fast as inflation (Morton, 1978). Also, many inefficient brewers left the business.

It is generally conceded, although systematic studies are rare, that consumers are sensitive to short-term changes in beer prices. A market survey in Southern California, for example, found that a price feature (reduction) can generate 10 times the average weekly volume in major brands of beer (Supermarket Business, May 1982, p. 44). Such evidence is ancedotal and does not report how much of a price decrease is needed to induce a ten-fold increase in volume, how much of the increase in volume represents new beer drinkers and how much of the increase represents beer drinkers who are changing brands.[10,11] Since each brewer produces many brands, the term inter-brand competition must be qualified when used to describe competition. The relevant issue is--is there competition among brewers, not is there competition among brands.

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[10] There is evidence that the demand for beer is such that observed increases in sales of one brand when the price of that brand is reduced is likely to be the result of consumers switching brands, rather than consumers switching from some other beverage to beer (Hogarty, 1972) (Horowitz, 1965).

[11] A particularly relevant statistic that is presently unavailable for an evaluation of the consequences of eliminating intra-brand competition would be information about the frequency of price features in areas with inter-brand and intra-brand competition versus the frequency in areas with only inter-brand competition.

To concede that some inter-brand competition exists is not the same as saying that inter-brand competition is strong enough so that policy-makers may be sanguine about granting brewers the right to establish exclusive territorial distributorships. This is because the strength of inter-brand competition may vary significantly from area to area.[12]

One characteristic that tends to blunt inter-brand competition at the local level is the distribution of more than one brand by distributors (Table 2). This practice has arisen because of inherent efficiencies in distributing beer and is particularly helpful to emerging brewers. As long as other distributors are free to enter a market, incentives exist for multi-brand distributors to price at the costs of production. If other distributors are not free to enter a market, multi-brand distributors--because they control the products of many brewers--are able to set price above costs and not face strong threats to their market share. Indeed, firms vending many brands are likely to have rather stable market shares (Meisel, 1981). As has been noted, if prices change and market shares remain stable, price competition is weak.

Another reason inter-brand competition is fragile is that market shares are already concentrated in the beer industry. The four largest brewers, for example, account for two-thirds of beer produced in the U.S. The 8 largest brewers provide over 90% of production (Table 3). Imports accounted for less than 4% of 1981 consumption (Miller, 1982). It may be

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[12] Alternatively stated intra-brand competition may be more important in some areas than others. Further, exclusive territorial distributorships, in the absence of market failure, bring about reduced incentives to innovate and produce efficiently; and the question of market coverage of low volume retailers is unresolved.

Table 2

Multi-brand Distributors in Selected Markets

Market	# of Distributors	# Distributors with More than One Brewer
Los Angeles	14	6
San Francisco	15	5
Portland (OR)	9	4
Seattle	12	2
Jefferson City (MO)	3	1
Lansing	8	3
Denver	7	2
Salt Lake City	5	2
Atlanta	8	3
Fresno	8	5
Phoenix	9	3
Albuquerque	8	2
Nashville	6	4
Columbia	4	2
Atlantic City	2	2
Pittsburg	66	57
Manchester	3	2
Miami	8	3
Birmingham	4	2
Peoria	5	3

Source: Beer Wholesaler Directory, 1980.

Table 3

Brewers' Estimated Market Share

	1979	1980	1981
Anheuser-Bush	26.8%	28.2%	29.8%
Miller	20.8	20.9	22.0
Schlitz	9.7	8.4	7.8
Heileman	6.6	7.3	7.7
Pabst	8.8	8.5	7.4
Coors	7.5	7.8	7.2
Stroh	5.6	5.5	5.0
Olympia	3.5	3.4	3.2
Others*	10.7	10.0	9.9

*Includes imports.

Source: John Maxwell, Beverage Industry, February 5, 1982.

concluded that at the national level there are few independent competitors. Further, there is evidence of economies of scale in brewing, tending to make entry into brewing difficult (Elzinga, 1971). Recent times have seen consolidations and mergers in brewing.[13]

It is true that market shares at the regional level may depart significantly from the national statistics because of the presence of regional brewers, the strength of competition among distributors and the buying habits of consumers. Nevertheless, the national statistics are telling.

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[13] In April 1982, Stroh and Schlitz merged with the approval of the U.S. Department of Justice providing that Schlitz attempt to sell one of its two breweries in the Southeast. In June 1982, Heileman made a tender offer for Pabst.

Even if there are some local markets in which market shares are not concentrated in the hands of a few, as a matter of arithmetic, there must be local markets in which market shares are more heavily concentrated. As a matter of fact, all brewers do not vend in all markets; thus, local shares must be higher than what national shares would indicate. For example, at the national level the combined market shares of Heilman and Pabst is about 15%. In Wisconsin and Minnesota, Heileman and Pabst together have more than 50% of the beer market (Wall Street Journal, June 1, 1982).

The Department of Justice reports that in 6 states, four firms control 90% of the market; in 30 states, four brewers account for over 80% of beer sales; and in 39 states, over 70% of beer sales are controlled by four brewers (April 13, 1982, correspondence from the Office of Legislative Affairs to the House Committee on the Judiciary).

Limited public evidence on beer distributor market shares was published in mid-1981 (Beverage Industry, July 24, 1981) showing that nationwide, 16% of beer distributors control 55% of total sales. Nine regional breakdowns were reported (See Table 4). It may be seen that at the regional level, large market shares are controlled by relatively few distributors.

The evidence so far indicates that at the national level large market shares are held by a few brewers and a small percentage of distributors. Available evidence indicates this is the case at the regional level for distributors. There is no readily available direct evidence at, say, the county level. But, again, as a matter of arithmetic, if there are local markets that are not dominated to the extent that national (regional) figures indicate, there must be local markets that are controlled to an extent greater than indicated by national statistics.

Table 4

Regional Market Shares for Beer Distributors

Region	Size (million of $)	# of Companies	(%)	Share of Mkt
New England	> 5	58	(38)	73%
	< 5	93		27
		151		
Mideast	> 5	142	(18)	64
	< 5	653		36
		795		
Great Lake	> 5	152	(16)	52
	< 5	825		48
		977		
Plains	> 2	229	(12)	75
	< 2	317		25
		546		
Southeast	> 5	152	(17)	52
	< 5	741		48
		893		
Southwest	> 5	80	(15)	54
	< 5	453		46
		533		
Rocky Mt.	> 5	81	(38)	71
	< 5	131		29
		212		
Far West	> 5	124		NA
	< 5	483		NA
		607		

Definitions:

New England: Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, Vermont.

Mideast: Delaware, District of Columbia, Maryland, New Jersey, New York, Pennsylvania.

Great Lakes: Illinois, Indiana, Michigan, Ohio, Wisconsin.

Plains: Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota, South Dakota.

Table 4 (continued)

Far West: Alaska, California, Hawaii, Nevada, Oregon, Washington.

Southeast: Alabama, Arkansas, Florida, Georgia, Kentucky, Louisiana, Mississippi, North Carolina, South Carolina, Tennessee, Virginia, West Virginia.

South West: Arizona, New Mexico, Oklahoma, Texas.

Rocky Mountain: Colorado, Idaho, Montana, Utah, Wyoming.

Source: Beverage Industry, July 24, 1981.

Concerns are voiced over large market shares held by relatively few firms because agreements concerning pricing may result. This type of pricing results in prices being set above the costs of production and is inconsistent with advances in consumer welfare.

Moreover, agreed upon pricing is facilitated by exclusive territories. First, exclusive territories eliminate intra-brand competition. As sources of competition are eliminated, it becomes easier to reach agreements.[14] Second, exclusive territories prevent a cheating member of a cartel from arguing that an increase in market share (the reward to cartel cheating) was the result of competition among his non-exclusive distributors (Posner, 1977).

Exclusive territiories have been shown to have an impact on the retail price of beer. Comparisons between states with exclusive territories and those without are frustrated by the above noted variation in taxing and other point-of-sale restrictions that tend to influence the retail price of beer. Information is available from the experience in

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[14] At the minimum, the number of two-way communication channels is reduced (Williamson, 1970).

Indiana. Indiana abolished exclusive territories in 1974. There are reports in trade publications that the average retail price of beer in Indiana has decreased in nominal terms (unadjusted for inflation) and relative to prices in neighboring Michigan (Beer Wholesaler, March/April 1981). The minutes of the Indiana Alcoholic Beverage Commission Study Committee reveals that wholesale and retail price decreases of 20% resulted from ending protected beer distribution markets (September 16, 1981, p. 4). This amounts to about a $2.00 decrease in the price of a case of beer.

There is theory and evidence to support the notion that the establishment of exclusive territories for the distribution of beer will place place upward pressure on prices. This is inconsistent with advances in consumer welfare.

2. Discrimination

Assuming differing price sensitivities among consumers of beer in different parts of the country reflecting variations in income, demographics, climate and the like, regional price discrimination by brewers would be advantageous to them. Intra-brand competition among distributors would prevent successful price discrimination by brewers; exclusive territories would suppress intra-brand competition and facilitate price discrimination.[15,16]

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[15] Laws requiring uniform FOB prices do not render price discrimination impossible. Transportation charges from brewers' dock to distributors dock may bring about significant variations in the C.I.F. price of beer to distributors. Further, advertising allowances and service differentials permit brewers to favor some distributors over others.

[16] If brewers can control where distributors may sell, they may be able to control to whom distributors may sell. Thus, the possibility exists that markets could be subdivided so that some distributors would serve only some outlets, others would serve others. This would tend to increase a brewer's ability to price discriminate.

Price discrimination redistributes purchasing power away from consumers to brewers. Economic analysis provides no standard for evaluating the welfare implication of this redistribution, although strong opinions are often voiced (Scherer, 1980, p. 320). It is impossible to determine if price discrimination impairs or improves efficiency without detailed market analysis. The circumstances under which efficiency is unaffected are unusual and may constitute little more than an academic curiosity (Yamey, 1974; Williamson, 1973).

3. Conclusions

Exclusive territories do not promote price competition. Indeed, by restricting entry and reducing the contestability of markets, exclusive territories place upward pressure on retail prices. Inter-brand competition in the beer industry is fragile. The current and desirable practice of a distributor carrying the products of more than one brewer helps consumers if markets are open. This practice can hurt consumers if markets are closed by facilitating pricing agreements. Regional price discrimination by brewers is facilitated and this has adverse distributional consequences for consumers.

C. Efficiency and Innovation

Consumers benefit when goods and services are produced at minimum average cost. As a business expands, average unit costs may stay the same (referred to as constant returns) or increase or decrease (referred to as non-constant returns). Non-constant returns may be illustrated by small volume distributors producing at higher unit costs than distributors with large volumes. Similarly, large volume dealers may grow too large and lose control of their operation. Constant returns may be illustrated by those distributors who, although they have different sized businesses, produce at roughly the same average costs.

The implications of this for exclusive territorial distributorships are as follows:

- o If as businesses grow, unit costs decline, the prospect of increased efficiency is raised by territorial expansion. If exclusive territorial distributorships prevent expansion, they reduce efficiency.
- o If as businesses grow, unit costs increase, inefficiency results unless other firms enter the market. If exclusive distributorships prevent other firms from entering a market (thereby forcing an existing business to grow too big), exclusive distributorships reduce efficiency.
- o If as businesses change in size, costs remain about the same, the efficiency effects of exclusive distributorships are not likely to be great.

The efficiency question, then, turns on how costs vary with output in beer distribution. Some evidence on this is reported below. More importantly, it is shown that if markets are open, the efficiency question is moot. If markets are closed, the efficiency question is real. Exclusive territorial franchises, by reducing the contestability of markets, reduce the ability of entrepreneurs to adopt the most efficient method of distribution.

Direct evidence drawn from the experience of beer distributors on how unit costs vary as volume increases is sparse. The industry press reports that rising fuel costs hurt low volume distributors more than their high volume counterparts (Beer Wholesaler, September-October 1981). Examples are given of large wholesalers holding down expenses by buying diesel trucks and/or switching to a pre-sell system but that these options are cost prohibitive for low volume distributors. This evidence suggests that average unit costs (per gallon or barrel, for example) vary with output--this industry exhibits non-constant costs at least over some volume of output. The evidence is not conclusive, however, because fuel is not the only input. There may be offsetting advantages to low volume distributors--fewer stops, shorter stops--that are not reflected in fuel consumption comparisons.

It is plausible that average unit costs decrease for some volumes of output, level off for a while and then begin to rise again.[17] If so, beer distribution may be said to exhibit both constant and non-constant costs. Indirect evidence drawn from econometric (statistical) studies of motor carriers indicate unit costs are constant over some volume ranges[18] (Friedlaender, 1980).

There is a wide range of sizes among established distributors (see Table 5) indicating any economies or diseconomies of scale are not strong. There is some statistical evidence that average costs are constant over some volumes of output. It seems reasonable to conclude that in the beer distribution industry there is a range of distribution volumes over which average costs are constant and there are volumes at either end of a spectrum that exhibit non-constant unit costs.

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[17] This results in the flat-bottomed U-shaped average cost curve, so familiar to students of economics.

[18] The studies indicate that shipment characteristics such as size and weight, length of haul and the prices of labor, capital and fuel are significant determinants of cost.

Table 5

Beer Wholesalers: Distribution by Size

Size (million of $)	# of Companies	% of National Wholesale Sales
50	8	2.8
25 - 50	28	6.1
10 - 25	258	26.1
5 - 10	466	20.2
3 - 5	681	15.7
2 - 3	1,112	16.1
1 - 2	1,035	9.0
0 - 1*	1,126	4.0
	4,714	100.0

*Includes 20 companies unable to be classified.

Source: Beverage Industry, July 24, 1981.

There is no guarantee that the territories carved out by brewers when awarding exclusive territorial distributorships will be efficiently sized; some may be too big, others too small. Moreover, the methods of adjusting exclusive territories to changes in market conditions are likely to involve high transactions costs. Mergers may have to be arranged and/or indemnification paid.

Moreover, as indicated above, distributors often handle the products of more than one brewer. There is no guarantee that the territorial designations of one brewer will be the same as another. This lack of coincidence among territories may force a distributor to operate an inefficient technology or forego adopting an innovative technology.

In a regime of exclusive territories, distributors who presently have a low volume territory or experience a reduction in demand are frozen in a declining market. Their enterprise may fail not because they were inefficient, but because they were not allowed to exercise their ingenuity. In other words, rigid territories do not provide for the success of the efficient.

Contestable markets, however, do insure efficient production, permit distributors to decide how many brands to carry and where to distribute them, and provide for the success of the innovative and efficient distributor.

The efficiency aspects of contestable markets may be illustrated as follows. Consider a distributor who can vend between 20 and 60 million barrels a year at an average cost of $1. If demand increases beyond 60 million barrels to 80 million barrels, average costs increase to $1.10. If markets are contestable, a new entrant can challenge the incumbent for the increase in demand. The entrant may use the same technology as the incumbent and distribute 20 million barrels for an average cost of $1. The entrant can continue to serve all future increases in market demand until both the entrant and incumbent are distributing 60 million barrels. In this way, contestability allows resources to be saved. If markets were protected, average costs would have risen.

The incumbent, of course, need not stand by idly; the incumbent can experiment with new methods of distribution to lower unit costs. A new way to service high cost, low volume accounts may be found and thereby place downward pressure on average costs.

In either event (contest or innovation) the increase in consumer demand is accomodated without an increase in unit costs to the benefit of all participants in the economy. Here, then, is the source of the benefit of keeping markets open to new entrants and the cause for concern over efficient resource use generated by protecting markets, in this instance with exclusive territorial franchises. While there is no guarantee that brewers can pick the efficient distribution territory in all the regions where its product is consumed, free entry into a market does provide such a guarantee.

D. Service Quality

Proponents of exclusive territorial distributorships claim that the increase in marketplace regulation will improve service quality. This claim rests on two propositions. One is that the increased revenues earned by distributors in protected markets will be used to support increased services to retailers and consumers.[19] The second is that the beer distribution industry is characterized by free-riding.[20]

1. Increased Service

The first proposition limits consumer choice by bundling possibly unwanted services with the purchase of beer. If a group of consumers want extra services those consumers should be able to choose to pay for the services. Consumers, for example, that want cold beer, a large selection, convenient shopping hours and the like, may seek out those retail outlets that provide the desired services and will pay for the extra services. Conversely, those consumers who do not want extra services may seek out "warehouse" retail stores. These consumers should not be required to accept and pay for services they do not want.

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[19] The specific types of services that might be provided include guaranteed arrival time at the store, weekend service, handling of special orders, service to low volume retailers (discussed in Section IV), cold storage, maintenance of large inventories and increased responsiveness to manufacturers' suggestions.

[20] Free-riding is said to occur in the provision of information through advertising and monitoring service quality.

Furthermore, there is no guarantee that the increased distributor revenues gained in protected markets will be used to support increased services. The distributor may pocket the increased revenues. Although brewers in a regime of exclusive territorial franchises would have fewer distributors to monitor, the size of the reduction is difficult to judge. If poor service is detected, what could the brewer do in such a regime that it cannot do in open markets? Indeed, in open markets retailers and consumers can act to correct service problems when they are detected.

In states with franchising laws, the threat of franchise loss for not providing services appears idle. In states without franchising laws the threat is more credible, but here it must be asked if there is a real problem. Have brewers been cancelling distributorships? How many? For what reasons?

At bottom, if market areas are open, the contest among a brewer's distributors for market share is sufficient to insure the level of service for which the consumer is willing to pay. This is because retailers with alternative sources of supply have an enhanced bargaining position for gaining improvements in point-of-sale service quality. Conversely, retailers receiving poor point-of-sale service quality from an exclusive distributor of a brand for which his customers have some preference only have the option of curtailing business. For a retailer dependent upon beer sales, this is not a ready option.

2. Free-Riding

The second proposition--that of free-riding--is a traditional rationale for increased public involvement in the marketplace. Questions to be answered when thinking about government regulation of the marketplace include:

- o Is there market failure?
- o Does the proposed regulation correct the failure?
- o Does the proposed regulation represent the best solution?
- o Does the proposed regulation produce net benefits?

a. Advertising

The information argument may be stated as follows. When there are two or more distributors of the same brand of beer in an area and one distributor advertises and the others do not, free-riding may occur. This is because advertising is information that is put forth to increase sales of a particular brand of beer. Advertising may result in the increased sales not only of the advertising distributor, but in the sales of all. In this way, the non-advertising distributor is able to appropriate (some of) the advertising distributor's effort.

It is apparent that this argument applies only to advertising that is paid for by distributors, rather than the manufacturer or the retailer, and is non-specific as to point-of-sale. If beer advertising is done by the brewer, it does not create free-riding problems at the distributor level.[21] All distributors would benefit. Beer advertising paid for by retailers directs the consumer to specific points-of-sale. The retailer captures the value it creates by dispensing price and service information through increased sales. It may be concluded that only advertising provided by distributors has any potential to create free-riding problems.

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[21] A substantial amount of money is spent on advertising by brewers. In 1980, Phillip Morris, the owner of the Miller Brewing Company, was the 4th leading advertiser and spent $356 million. Anheuser-Busch spent $181 million and ranked 21st. Schlitz spent $66 million on advertising.

Distributor advertising need not create free-riding problems. Advertising paid for by one distributor may affect the sales of another distributor only if that information is non-specific as to point-of-sale. The free-riding problem in the provision of information results from a defect in an advertising message, not from a defect in market structure.

The quantitative significance of distributor advertising is difficult to judge. There seems to be no readily available figures on advertising by distributors. One has to interpret any figures that may become available somewhat cautiously. First, advertising may be paid for by distributors but the distributors may be reimbursed by brewers. Second, some distributor advertising is not appropriated by competing distributors because it is specific information (displays in taverns and the like). The industry press reports that retailers' purchase decisions are made on the basis of dependable service, rather than only on the image of the brand. (Beverage Industry, June 23, 1978). This suggests that advertising is not all important to distributors.

Even if there were free-riding problems in the provision of beer advertising, it is doubtful that exclusive territorial franchises would correct the failure. The "problem" arises because information "is given away free to consumers" in the media. To correct the problem, exclusive territories would have to be the size of media markets. There is no reason to believe that the optimal sized media market is the same as the efficient sized distribution area. Even if media markets and beer markets were coincident, informational externalities could be corrected through specificity in advertising. Finally, it must be shown that the free-riding problem causes more harm to consumer welfare than the harm--in the form of higher prices and reduced efficiency--caused by exclusive territorial distributorships. The harm caused by free-riding would be a reduced level of beer advertising. It is difficult to value the worth of a beer advertisement to a consumer; some may be redundant and confusing. The really useful advertising is price advertising that tends to be location specific and does not involve free-riding.

4. Product Quality

Although beer does not have an unlimited shelf life, the shelf life of beer is long.[22] Freshness is maintained by rotating old beer to the front of the shelf. (This is the standard practice for all perishables including meat and dairy products.) It is the responsibility of all (brewers, distributors, and retailers) to remove stale beer from the shelf.

If the distributor is non-local or if there is more than one distributor in an area, then one distributor may have to police a store served by another distributor and, in the extreme, remove stale products placed by a competitor. In this way, one distributor may impose costs on another, creating a free-riding problem.

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[22] The exact shelf life varies with different beers. Anheuser-Busch draft beer has a life of 45 days, as does Pabst draft. Packages have longer shelf life with Schlitz, Pabst and Miller reporting shelf life of 120 days, and Anheuser-Busch of 75-105 days. The shelf life of beer can be affected by light, heat and air. (Indiana Alcoholic Beverage Study Commission, August 11, 1981, Minutes).

A related problem occurs if the consumer buys stale beer. This damages the reputation of all (brewers, distributors and retailers). If there were only one distributor, the argument goes, more care would be taken in insuring that all stale beer were removed from the shelf.

As to the first problem, three questions must be asked. Why is it impossible for the distributor who vended the product that went stale to pay for the removal? Are exclusive territorial distributorships the best way to correct problems of this kind? What is the quantitative significance of the stale beer problem?[23]

Beer may go stale anywhere along the distribution channel from brewer to consumer. Exclusive territorial distributorships are suppose to correct free-riding problems occuring on the link between the distributor and retailer.[24] Most brewers use a code date that indicates the period of time over which the beer is likely to be fresh. If retailers are able to read the code, retailers will be in a position to reject beer that is likely to become stale before it is sold and consumed.

Even the most conscientious retailer may misjudge the buying habits of the consumer and have beer go stale. The retailer served by many distributors has a choice as to which distributor takes back the stale beer. This is said to create a free-riding problem.

It may be argued that beer may appear in retail outlets and that no local distributors vended the product to the outlet. The "mystery beer" is now stale. Who is responsible?

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[23] Industry-wide data on the amount of spoiled beer as a share of total is not available. Telephone interviews conducted with buyers for retail outlets indicated that spoiled beer is not now, and never was, a problem.

[24] Stale beer arriving from the brewer could be rejected by the distributor.

A solution to any potential stale beer problem is for the brewer to reimburse the distributor for the expenses involved in removing stale beer. In this way, it does not matter which distributor removes the beer since either would be reimbursed. Indeed, it would be to the brewer's advantage to have the most efficient distributor remove the stale beer, even if it were placed by the competing distributor.

It may be seen that free-riding problems, occuring in the distributor-retailer link of the distribution channel, may be diminished by instituting a way for retailers to know the remaining shelf life of the product placed in their outlets. Second, the problem can be eliminated by having the brewer accept responsibility for expenses involved in removing stale beer.

The second type of free-riding occurs when the consumer purchases and consumes stale beer. The reputations of all involved are damaged because of the carelessness of one or more of the participants along the distribution channel. Clearly, the way to reduce the significance of this problem is open dating. By stamping a date on the package that the product is good until some date, the consumer receives all the information necessary to make a decision about freshness. It does not profit a brewer to stamp an unreasonably distant date on the package, lest the consumer believes the brewer and purchases and (partially) consumes stale beer.

It may be concluded that the cause of this type of free-riding is a lack of information at the point-of-sale about product freshness. Open dating would fill that information gap. Further, exclusive territorial distributorships only would reduce the number of businesses whose reputations were harmed by a load of stale beer reaching the consumer.

It is arguable that the irresponsible party, whose carelessness resulted in the bad beer reaching the consumer, would shirk responsibility under any regime. Open dating would provide the consumer with the final responsibility for inspecting for freshness.

IV. Social Goals and Exclusive Territorial Distributorships

It is claimed that exclusive territorial distributorships will promote "a nation of small businesses" by protecting distributorships that are small businesses and by ensuring service to retail outlets that are small businesses.

An exclusive territory, the argument goes, will permit a low volume retail outlet to be serviced for the same price as high volume outlets. Since some low volume outlets cost more to serve than high volume outlets, absent exclusive territorial distributorships, this may not happen.

There are several responses that may be made to this argument. First, low volume beer retailers need not be small businesses and high volume beer retailers may be small businesses. Accordingly, the ideal of a nation of small businesses may not be facilitated by the cross-subsidy of low volume beer retailers (a drug store chain that carries beer) by high volume beer retailers (a "mom and pop" store). It should also be pointed out that beer distributors who would be protected from competition may or may not be small businesses. In fact some are and some are not (see Table 5, above).

Second, retailers that are costly to service consume more of society's scarce resources than providing service to less costly accounts. Efficient resource use and consumer welfare are advanced by charging higher prices for products and services that are costly to provide.

Third, there is no guarantee the exclusive territorial distributorship will service the low volume account. The protected distributor will have an incentive to overcharge and restrict output. The reduction in output may take the form of reduced service to high cost outlets. Some high cost outlets are low volume outlets and some low volume outlets are small businesses. Exclusive territorial distributorships, then, are inimical to the needs of some small businesses.

Fourth, the social goals of promoting small businesses may be advanced by other means. Open markets provide incentives to service all accounts. Low volume outlets--be they "mom and pop" businesses, taverns or affiliates of large chains that merchandise a variety of products--exist because there is a demand for their services. There are some characteristics that the low volume retailer offers to consumers that consumers find valuable. In providing beer to customers, the low volume retailer has to pay the cost of distributing beer to his location. Paying for service, however, is consistent with advances in consumer welfare.

Markets allow for changes in demand to be reflected on the supply side. Inefficient distributors may fail; efficient distributors may thrive. It may happen that the distributor that fails is small and the one that thrives is not. If it is social policy to promote small businesses, then it needs to be shown that exclusive territorial franchises are the best way to achieve this goal. The alternatives of direct subsidy or tax expenditure, at the least, would place social policy under the control of Congress rather than beer distributors.

V. Conclusions

Some of the nation's 4,700-plus beer distributors have exclusive territorial distributorships and some do not. In either event, beer appears to be distributed throughout the nation (wherever it is legal to do so) without any noticable problems. There has not been any situation analogous to the energy crisis with its long gas lines, and rapidly increasing utility bills. Nevertheless, legislation was introduced into the 97th Congress to impose additional regulations on beer distributors by permitting brewers to grant exclusive territorial franchises.

The focus of this report is the effects that exclusive territorial distributorships are likely to have on consumer welfare. Exclusive territorial distributorships reduce the ability of entrepreneurs to enter a market and, in so doing, forestall advances in consumer welfare. It might be possible for exclusive distributorships to advance consumer welfare if there is a free-rider problem in the distribution of beer; but only if exclusive territories will correct the free-rider problem in an efficient and beneficial way.

Quantitative assessments of the effect of exclusive territorial distributorships on consumer welfare are made difficult by variations in state regulation and data availability. However, the experience of one state and the application of economic theory lead to the following conclusions.

Price competition would be blunted by the establishment of exclusive territorial distributorships. The consequence of this is retail prices that do not lie close to costs. This means that consumers must sacrifice more value than they receive. This is inconsistent with advances in consumer welfare.

Exclusive territorial distributorships facilitate a redistribution of purchasing power away from consumers, towards brewers. This could be accomplished by regional price discrimination. Although there appears to be nothing illegal with this practice, the political implications of facilitating it are telling.

Efficiency, as indicated by producing a minimum average cost, in any industry and particularly in the beer industry, is guaranteed in open markets and occurs only fortuitously in protected markets. Of particular importance is the inflexibility to changing market conditions occasioned by exclusive territorial distributorships.

Innovation in beer distribution may go unrewarded in exclusive territories because firms are frozen into particular areas. Contestable markets, on the other hand, permit entrepreneurs to exercise their ingenuity and provide for the success of the efficient.

The argument--that exclusive territories for the distribution of beer will increase the level of service provided to consumers--is really an argument to force some consumers to purchase services they do not desire. Retailers are more likely to gain improvements in point-of-sale services when there are contests for their business than when they have no choice.

The free-riding problem involving the provision of product information by beer distributors is trivial, unlikely to be solved by exclusive territories and more efficiently solved by "smarter" advertising.

Similiarly, the free-riding problem involving the monitoring of product quality by beer distributors is trivial, unlikely to be solved by exclusive territories, and more efficiently solved through open dating.

The use of beer distributors to promote social goals is dubious social policy. Further, small businesses may or may not be low volume retailers and low volume retailers may be big business. In the extreme, a high volume, "mom and pop" beer business may subsidize a low beer volume chain store. Finally in the beer industry, the market works to provide incentives to serve small business.

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Senator **Laxalt**. We will now hear from the Department of Justice, the Deputy Assistant Attorney General, Abbott B. Lipsky, Jr. Mr. Lipsky, welcome to the committee.

STATEMENT OF ABBOTT B. LIPSKY, JR., DEPUTY ASSISTANT ATTORNEY GENERAL, ANTITRUST DIVISION, U.S. DEPARTMENT OF JUSTICE

Mr. **Lipsky**. Thank you very much, Mr. Chairman.

My first job out of law school was the easiest job in the world. As an attorney at the Antitrust Division, I was assigned to go up to the Civil Aeronautics Board and persuade the Board to adopt competitive principles. Inasmuch as Fred was the chairman then, you see why I characterize that as the easiest job in the world. I also had the privilege of serving on the staff of the National Commission for the Review of Antitrust Laws and Procedures, of which Fred was a member. Also, I served as Fred's special assistant for regulatory reform when he was in the White House with President Carter.

I agree with Senator Proxmire; his prediction was correct. Fred made a mistake, I don't mean the same mistake, though. We also oppose S. 1215, although for slightly different reasons than Dr. Kahn just enunciated.

I am somewhat surprised coming up here and listening to the testimony and Senator Proxmire's remarks. I had not thought that the bill was a States rights bill. The word State appears only very sparely in the draft that I have. I think I would have to agree with Dr. Kahn on the issue that you last questioned him on, Mr. Chairman, that one does not need State adoption or conformance of their law to the provisions of S. 1215 for this exemption to apply. It says, in terms, that no antitrust law shall prohibit, or render unlawful the inclusion and enforcement in any written contract, et cetera, et cetera, of an exclusive territorial arrangement between the brewer and the distributor.

It does not seem to me that the provisions of section 2 of S. 1215 need any State enactment to trigger them.

However, I wonder if the point of confusion is not over the existence of the case, *Rice* v. *Williams* currently under submission to the Supreme Court in which the State of California attempted to cut the Oklahoma connection with a statute which a State court held unlawful under Federal antitrust principles. As I say, that case is under submission to the Court. You mentioned the case earlier, I believe, in your opening remarks, Mr. Chairman. If you want to find out why the Supreme Court will reverse that State court result—and I agree it is an undesirable result—I invite you to read the brief the United States submitted on that point to the Supreme Court some months ago. I fully expect that the court will correct the mistake made by the State court in *Rice* v. *Williams*.

Senator **Laxalt**. What is the status of that before the Supreme Court?

Mr. **Lipsky**. I am just told it has been orally argued. Briefs were submitted some time ago. So, we are awaiting a decision.

Senator **Laxalt**. Do you think we will have a decision this term?

Mr. LIPSKY. I hesitate to predict the timing, but there is no further step to be taken unless the court asks for it. But at this moment we expect a decision in the case.

Senator LAXALT. I think it would be helpful to us, I do not see it here anywhere in the files, for Justice to provide us with a recap of the contentions in that particular proceeding so that we know what is before the court. I think that would be helpful.

Mr. LIPSKY. I am sure that we can use the expertise of the Solicitor General's office and our own appellate lawyers and comply with that request in short order, Senator.

The Department of Justice——

Senator LAXALT. Staff points out to me that it is not clear whether or not this proposed legislation would impact that particular case or not. Perhaps you could touch on that as well and indicate what you believe to be the linkage.

Mr. LIPSKY. I will endeavor to do that, Mr. Chairman.

The Department of Justice's position on S. 1215 simply is that it is addressed to a problem which does not exist. Even if the problem did exist, this bill would not solve it. The Supreme Court made abundantly clear in *Continental TV* v. *GTE-Sylvania*, which you mentioned in your opening statement, Mr. Chairman, that the law applied to vertical territorial restrictions is the so-called rule of reason. I will subscribe to Dr. Kahn's description of the rule of reason, but suffice it to say that it is just an antitrust lawyer's fancy way of saying that the courts balance the factors on one side and balance the factors on the other in determining whether any particular practice is on balance anticompetitive or not.

Senator LAXALT. Has that as a practical matter resulted in differing balancing and differing criteria among the various circuits?

Mr. LIPSKY. I think inevitably it will, but there is no disagreement as to the basic outlines of the test. Indeed, I think the lower courts have done quite well. We cite in our letter which we sent up on April 13, and again briefly in my written testimony, the situations in which courts have taken seriously the procompetitive justifications for the use of exclusive territories in this industry. We think that on balance the lower courts are doing rather well.

I would point out for the committee in particular the recent decision in *Valley Liquors, Inc.* v. *Renfield Importers*. This is the first antitrust decision written by Judge Richard Posner since his appointment to the seventh circuit by the current administration. There you will find as cogent and clear, I believe, a statement of the current state of the rule of reason analysis as one can find in contemporary law. The test is clearly articulated, that one balances the effects on interbrand and intrabrand competition. The case is in an industry very closely related to the malt beverage industry; namely, I believe it involved a distributor of wine and distilled spirits. There the possible procompetitive benefits of exclusive distribution systems are explained quite cogently. The present leadership of the Antitrust Division in the Department of Justice, as you know, is quite sympathetic to that type of analysis. We believe that Judge Posner articulates the correct analysis.

It is difficult for us to see why there is any confusion about this particular issue. Even if there were confusion, I am not sure that this bill really goes very far in clearing it up. It uses language that differs from that used by the Supreme Court in *GTE-Sylvania*. It talks about a requirement for "substantial and effective" competition. I am sure that in the various cases that would be brought around the country on the basis of that language one would need to go through a process of interpreting that provision to determine what is substantial and effective competition in any given context or in any given market.

What we are really looking at, if we should end up with this bill, is a long process similar to the nearly century-long process which we have now, in which the simple language of the Sherman Act, which speaks in terms of restraints of trade, has been spun out and interpreted a number of times by the Federal judiciary. We are finally now getting to the point where that analysis seems to have been put, at least with respect to exclusive territories, quite properly and succinctly in order by the *GTE-Sylvania* decision.

I would submit that, if one were to look back at any particular moment in history and ask when confusion over the antitrust standard was at its minimum, one would have to say the present moment. The law seems to be applied fairly consistently across the circuits. The principles enunciated are simple and are being correctly applied, for the most part. As I say, one does get an aberrational case such as *Rice* v. *Williams*, which we are confident the Supreme Court will correct in short order.

Let me close simply by addressing myself to what I believe is Dr. Kahn's mistake——

Senator LAXALT. Before you move onto that, do I understand these recent comments are all directed to one central point you want to make to this committee? You do not think there is any necessity for this at all, and we can operate within the existing framework using the rule of reason as the rationale? And you think that has been working reasonably well in the country without this kind of corrective legislation?

Mr. LIPSKY. Certainly in this industry it has, yes.

Senator LAXALT. Is that essentially the point that you want to make to this committee?

Mr. LIPSKY. Yes, that. Also, the second point is that, even if one perceived the necessity, I do not believe this bill would go very far to clear up any confusion. It introduces a number of words and phrases, terms of art which will require a definition over a long process of common law interpretation over the years. So, as much confusion is likely to result from the standards stated in this bill, which is a very general standard as has resulted from the standard stated in the Sherman Act, which has been around for a long time.

The final point, as I say, to specify the mistake I think Dr. Kahn made, is in his hostility on competitive grounds to the idea of the use of exclusive territories. I believe Dr. Kahn unjustifiably minimizes the utility of exclusive territories. I think it is perfectly evident that one should not equate all types of price-reducing behavior as necessarily good. There are parasitic forms of competition which one witnesses at a flea market where stolen goods are traded. Indeed, the investment made by appointed distributors in other industries of whatever inputs they care to contribute to the sale-promoting process, be it advertising, be it quality control, be it customer education, whatever form that takes, does represent an investment by the distributor. If the manufacturer believes that it is warranted under the market conditions, he should be expected not to pirate the efforts of others by failing to make those investments himself and reflecting his failure to make those investments at a lower price, that is a parasitic form of competition under some circumstances. Indeed, it is the likelihood of these circumstances occurring in this industry that accounts for our position on this bill. Under some circumstances the use of exclusive territories can give rise to potential problems of collusion that we would characterize as truly anticompetitive problems.

It is to preserve our option to attack those anticompetitive circumstances where they may arise that we oppose this bill. It would deprive us of those options.

I think at that point, Senator, I would just like to invite the committee's questions.

Senator LAXALT. Thank you very kindly. Tell me, would you have these same basic objections to the soft drink legislation?

Mr. LIPSKY. Well, the soft drink industry is a very different one, where you have the local franchisee actively involved in the production process for the basic product. There are similar concerns which the Department of Justice expressed at that time, I understand. But the industries are not identical.

What we are trying to speak to in our objections to S. 1215 is the fact that in this particular industry one finds circumstances that render it especially susceptible to anticompetitive results in the presence of widespread use of exclusive territories. That is detailed in my written statement as well as in the letter. We have high concentration at the national level, high concentration at the wholesale level. We have a homogeneous product. We have a relatively high transportation cost industry. We have all kinds of grounds for believing that collusive arrangements can be easily arrived at and relatively easily policed in this industry. That is not to say that we believe that collusive arrangements are widespread or that they are occurring at any particular point in this industry, although we have had experience with collusive arrangements in this industry at the distributor level in the past. I refer to our case in Hawaii. But because of circumstances in this particular industry, it is rendered especially susceptible to collusive outcomes from the widespread use of exclusive territories.

We oppose this bill.

I have simply not looked with the same degree of care at the soft drink bottlers bill, although I know that expertise resides within the division. I would be glad to render any comparison of them that you feel is appropriate.

Senator LAXALT. I think it would be helpful. As a matter of policy, we did move into the soft drink industry. In the judgment of many of our colleagues, there is great similarity in these two pieces of legislation in that respect.

Tell me, as far as Justice is concerned, what has been the experience of the soft drink industry? Has this developed into collusive practices or any other questionable results?

Mr. LIPSKY. Nothing comes immediately to mind. I would be glad to look into that.

Senator LAXALT. That would be helpful——

Mr. LIPSKY. The Federal Trade Commission——

Senator LAXALT [continuing]. To see what the experience has been as far as Justice is concerned, as far as soft drinks are concerned.

Mr. LIPSKY. I will look into that, Senator. My suspicion is that the Federal Trade Commission has tended to assume a leading role with respect to practices in that particular industry.

As I say, we did have one case out in Hawaii in which we had a beer brewer encouraging its distributors to fix prices among themselves. It benefited from that collusive arrangement by raising the wholesale price to those distributors, which seemed to confirm our fears that the product characteristics in this industry were such that collusive arrangements were attractive economically. We sought in that situation to make sure that they were made unattractive by virtue of our enforcement powers.

Senator LAXALT. Well, if you can give us what experience has been from the Justice perspective, we will be in touch with the FTC. Their wings have been substantially clipped, as you know, but we will find out what, if anything, they have been doing.

Mr. LIPSKY. I am sure they can still fly.

Senator LAXALT. Last, you said that, irrespective of what policy we adopt here, there are problems with the particular wording of this legislation. Although it does not signify any commitment on the part of this committee, it would be helpful if you would give us constructive suggestions in connection with improving the wording in the event we decide to go forward.

Mr. LIPSKY. I will address that question, Senator, although I suspect our response is likely to refer to some of the better formulations that came up in the *GTE-Sylvania* case, for example, or in the *Valley Liquors* case that I have just been discussing. The difficulty here is that the real merit of the antitrust standard is that it is a generally valid standard very difficult to reduce to specific terms that would make it generally applicable to all industries. One relies to a certain extent on the sensitivity of the Federal judiciary to give content to those general standards as they have to the basic language used in the Sherman Act itself, which speaks in terms of restraint of trade.

So, it is a matter of adopting a very special formulation for one particular industry. It is that process itself which, in essence, is part of the basis for our objections. As we warned when we opposed the soft drink bottlers bill, this will be cited in support of other piecemeal antitrust special rules, which are going to deprive the antitrust laws of much of their utility.

It was interesting to hear Senator Proxmire citing the soft drink bottlers bill for exactly that proposition. If there is some general aspect of the antitrust laws or private treble damage actions or Government antitrust enforcement that somehow makes Federal courts go crazy and reach what is later perceived to be crazy results or inappropriate results, we are entirely open to discussing general reforms, either making general suggestions for broad-based shifts in judicial interpretations of the antitrust laws or even suggesting specific legislation. But it is the general applicability of the basic rule of reason standard which renders it so useful and so comprehensible. So, I think it has served very well the longrun efficiency and productivity of the American economy.

That is not to say there are no decisions in all of antitrust jurisprudence with which we would disagree. They are numerous, and Mr. Baxter has not been shy in pointing out which ones those are. But, if we perceive a problem with the judiciary's interpretation of these laws, let us fix it for everybody, not just for this special group.

Senator **Laxalt**. You have made your point well. We thank you very much.

In all probability, we will have some written questions for Justice.

Mr. **Lipsky**. We will be glad to respond to those as well as the various questions you have put to me today, Senator. I thank you for the opportunity to testify.

Senator **Laxalt**. Thank you. Without objection, we will place your prepared statement in the record.

[The prepared statement of Mr. Lipsky and subsequent answers to queries of the committee follow:]

Department of Justice

TESTIMONY

OF

ABBOTT B. LIPSKY, JR.
DEPUTY ASSISTANT ATTORNEY GENERAL
ANTITRUST DIVISION

BEFORE THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

CONCERNING

S. 1215
THE MALT BEVERAGE INTERBRAND COMPETITION ACT

ON

JUNE 21, 1982

Mr. Chairman and Members of the Committee:

I am pleased to appear this morning to present the views of the Department of Justice on S. 1215, the "Malt Beverage Interbrand Competition Act." As you know, the Department submitted a comprehensive letter on April 13, 1982, detailing the grounds for our objections to this legislation. I will not repeat all of what appears in that letter (a copy of which is attached for your convenience), but I would like to highlight our major objections.

Essentially, the bill states that exclusive territorial agreements between wholesale distributors and brewers, importers, trademark owners, or trademark licensees of malt beverages shall be deemed lawful under the federal antitrust laws so long as the malt beverages covered by such agreements are in "substantial and effective competition" with other such products within a defined geographic area. While we recognize that this language is intended to "clarify" the applicability of the antitrust laws to exclusive dealing arrangements in this industry, no such clarification is needed. The Supreme Court adopted an entirely sensible rule of reason approach to exclusive vertical territorial agreements in Continental T.V., Inc. v. GTE Sylvania, Inc. */

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*/ 433 U.S. 36 (1977).

That approach embodies a correct judicial recognition that such arrangements are not necessarily -- or even typically -- anticompetitive, although they may have anticompetitive effects and may therefore violate Section 1 of the Sherman Act in certain limited circumstances.

Further evidence that clarification of the law in this area is unnecessary is the recent decision of the Seventh Circuit Court of Appeals in *Valley Liquors, Inc.* v. *Renfield Importers, Ltd.* */ There, Judge Posner clearly recognized that the legality of a distribution arrangement between a supplier of wines and liquors and its exclusive wholesale distributors was subject to the rule of reason, and that the arrangement would not unreasonably restrain trade unless, "weighing effects on both intrabrand and interbrand competition, it made consumers worse off." **/

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*/ 42 B.N.A. Antitrust & Trade Reg. Rptr. 1185 (7th Cir., decided May 21, 1982).

**/ *See also* Del Rio Distributing, Inc. v. Adolph Coors Co., 589 F.2d 176 (5th Cir.), *cert. denied*, 44 U.S. 840 (1979), in which the Fifth Circuit Court of Appeals upheld a jury verdict that Coors' exclusive territorial restrictions were reasonable because there was ample evidence showing that the territories "were essential to maintaining quality control and service in the retail market" and resulted in "a long-term effect of making each distributorship stronger, better able to compete with other brands and provide better service." 589 F.2d at 179. Additional post-*GTE Sylvania* cases recognizing the beneficial effects of vertical territorial arrangements are cited in our letter to the Committee on this bill at p. 12, note 9.

Even if legislative clarification of the law were necessary, if enacted, S. 1215 is more likely to confuse than to clarify the law. This is because the bill contains language different than that generally employed by courts in stating the rule of reason, and hence, creates the risk that the bill could be interpreted as creating a different and perhaps weaker standard for judging the legality of exclusive territorial arrangements in this industry than that articulated in GTE Sylvania.

The Department of Justice recognizes that the use of exclusive territorial arrangements by manufacturers is usually motivated by a desire to overcome free rider effects among distributors or wholesalers, or to create a specific point-of-sale environment, and that when so motivated, they generally have beneficial effects. In the malt beverage industry, for example, distributor expenditures on product promotion enhance the value and reputation of the product, leading to increased sales of the product and intensification of interbrand competition. However, the malt beverage industry is a textbook example of those very special circumstances in which widespread use of exclusive territorial arrangements might have anticompetitive effects. First, concentration at the manufacturing level is very high: In 1980, the top two brewers had a combined national market share of 50.0 percent and the top four had 67.1 percent.

Concentration at the state level was often significantly higher than national concentration, with four-firm concentration levels exceeding 80 percent in the great majority of states for which information was publicly available. */ Second, the malt beverage distribution system translates high brewer concentration into high concentration at the wholesale level. Virtually all brewers use exclusive territorial arrangements and, in many markets, different brewers utilize the same wholesaler. Thus, concentration at the wholesale level may exceed that at the brewer level.

Where exclusive territories are employed by most or all brewers selling in any particular market, concentration may reach levels where collusion among distributors becomes a realistic threat. While wholesaler collusion is usually not in the manufacturer's interest because it increases wholesale prices and markups while reducing manufacturers' sales and profits, manufacturers might not seek to deter wholesaler collusion if they believed they could share in the higher profits earned by colluding wholesalers, perhaps by raising wholesale prices, charging franchise fees, or imposing other obligations on wholesalers. Furthermore, collusion

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*/ See 1981 Modern Brewery Age Blue Blook; Steinman's Beer Statistics News, April 1981. This market share data is more fully discussed in the Department's letter to the Committee at p. 6, n.4.

may be easier at the wholesaler than at the manufacturer level, and might be more difficult to detect than in other industries, since wholesaler collusion would probably take place on a localized scale.

Ordinarily, of course, a variety of factors offset the risk of collusion from this source -- even in concentrated markets. For example, ease of entry into distribution would allow existing manufacturers to undercut any collusion among distributors. If entry into manufacturing were also easy, a new entrant could quickly exploit the opportunity for new sales created by the high prices and restricted availability of other manufacturers' products resulting from wholesaler collusion. This could take the form of manufacturer integration downstream to create new distributors, luring existing distributors away from the collusive scheme, or inducing the entry of new independent distributors.

Unfortunately, the peculiar characteristics of the malt beverage industry suggest both high risks of distributor collusion and the absence of these mitigating factors. Concentration is high at the distribution level; the product is relatively homogeneous; state regulation often compels advance public announcement of prices and adherence to those prices; state regulation usually prohibits vertical integration by brewers into wholesaling, and erects barriers to entry by independent wholesalers; finally, entry at the brewing stage does not seem easy.

This combination of factors not only creates an unacceptably high risk that wholesaler collusion may occur in this industry, it also tends to diminish the likelihood that manufacturers would seek -- or be able -- to deter or defeat wholesaler collusion. Because enactment of S. 1215 could result in an antitrust standard less flexible than the rule of reason, we strongly oppose its enactment.

Moreover, we strongly oppose enactment of single-industry antitrust rules. If clarification of existing law concerning exclusive territories is necessary, then it should be made on a general basis through judicial interpretation of existing antitrust laws or through congressional enactment of standards of general applicability. So-called legislative "legitimization" of exclusive territorial arrangements in the malt beverage industry is additionally undesirable because it might be construed to imply -- quite incorrectly -- that such arrangements are less legitimate in industries not affected by this legislation. Finally, enactment of additional special-interest antitrust legislation would cast further doubt on the universal applicability of the antitrust laws to the unregulated sectors of our economy and invite other industries to seek similar legislation.

This could only lead to a patchwork of differing antitrust rules that would greatly complicate antitrust enforcement and deprive the antitrust laws of much of their utility.

In conclusion, Mr. Chairman, enactment of S. 1215 would be unnecessary and unwise. I thank the Committee for its attention, and I would be happy to respond to its questions.

Attachment

U. S. Department of Justice
Office of Legislative Affairs

Office of the Assistant Attorney General

Washington, D.C. 20530

APR 13 1982

Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
Washington, D.C. 20515

Dear Mr. Chairman:

This is in response to your request for the views of the Department of Justice on S. 1215, the "Malt Beverage Interbrand Competition Act."

The bill's stated purpose is "[t]o clarify the circumstances under which territorial provisions in licenses to distribute and sell trademarked malt beverage products are lawful under the antitrust laws." Section 2 of the bill provides that nothing contained in any federal antitrust law shall render unlawful exclusive territorial agreements in any written contract between a wholesale distributor and any brewer, importer, trademark owner, or trademark licensee of a trademarked malt beverage, 1/ so long as the malt beverages covered by such agreements are in "substantial and effective competition with other malt beverage products within [a] defined geographic area." Section 3 provides that nothing in the bill shall be construed as legalizing enforcement of such exclusive territorial arrangements by means of "price-fixing agreements, horizontal restraints of trade, or group boycotts, if such agreement, restraints or boycotts would otherwise be unlawful."

The Department strongly opposes enactment of this legislation. The bill might be interpreted as creating a different standard for judging the legality of exclusive territorial arrangements in the beer industry, a standard

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1/ "Malt beverage" is defined in section 5 of the bill as "beer . . . ale, porter, stout, and all other similarly designated fermented beverages containing one-half of one percentum or more alcohol by volume."

weaker than that articulated in Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36 (1977), and currently applicable to most industries.

A different, weaker standard for judging exclusive territorial arrangements in the beer industry is undesirable for two reasons. First, although exclusive territorial arrangements usually serve efficient purposes, the beer industry is a good example of those very special circumstances in which widespread use of such arrangements might have anticompetitive effects. Second, and more important, as a general policy the Department opposes piecemeal, special-interest changes in antitrust standards of general applicability. To the extent that any clarification is required of existing law towards exclusive territories, such clarification should be through judicial interpretation of existing antitrust legislation or through Congressional enactment of broadly applicable standards regarding territorial distribution provisions.

We shall develop these points in turn. First, we shall restate our present position towards exclusive territories, noting that they usually serve legitimate purposes, but might be used for anticompetitive purposes in certain special circumstances. Then we shall outline precisely these special circumstances and show that they are often present in the beer industry. Finally, we shall discuss present doctrine involving exclusive territories and the likely effect of the proposed legislation.

The use of exclusive territorial arrangements by manufacturers is usually motivated by a desire to overcome free rider effects among distributors (wholesalers). In many industries, distributor expenditure on product promotion, quality control (e.g., the refrigeration of beer while in storage), or point-of-sale services enhances the value and reputation of the product, leading to increased sales of the product and intensification of interbrand competition. If several distributors can sell a manufacturer's product in a given geographic market, they all benefit from the enhanced reputation of the product and the associated increase in sales induced by the expenditures of any one distributor. That distributor would capture only a fraction of the increased sales induced by its own expenditures. The result would be too little expenditure in the aggregate on product promotion, quality control, or point-of-sale services, since any one distributor would be reluctant to spend heavily so long as others were able to "free ride" by taking advantage of sales increases without contributing to the expenditures responsible for those increases. To encourage expenditures, a manufacturer may award exclusive territories to its distributors--assign a different geographic area to each distributor and permit only the designated distributor to sell in its assigned area. Promotion, quality control, and point-of-sale services will increase, the reputation of the product will improve, and sales of the product will increase. Where exclusive territories are awarded to combat free rider problems and improve the product's reputation, the economic effects are generally beneficial. 2/

The Department recognizes that exclusive territorial arrangements have beneficial effects in a wide range of market settings. Therefore, the Department views such arrangements as legitimate in most cases. They are prohibited only where their effect may be substantially to weaken interbrand competition. One way in which exclusive territories may weaken interbrand competition is by facilitating collusion among wholesalers. Widespread use of exclusive territories by all or most manufacturers may reduce substantially the total number of wholesalers competing in any geographic area. Since the likelihood of collusion increases when the number of firms in the market is reduced to a very small number, widespread use of exclusive territories may weaken interbrand competition, by facilitating collusion among wholesalers of the different manufacturers.

It might be argued that manufacturers would not award exclusive territories for the purpose of facilitating wholesaler collusion, since such collusion increases wholesale prices and markups while reducing manufacturers' sales and profits. However, manufacturers might desire wholesaler collusion if they believed that they could share in the higher profits earned by colluding wholesalers. 3/ Furthermore, collusion may be easier at the wholesaler than at the manufacturer level. The number of wholesalers in any given area may be lower than the number of manufacturers because

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2/ For a more detailed discussion of the free-rider argument, see Richard A. Posner, "The Rule of Reason and the Economic Approach: Reflections on the Sylvania Decision," U. Chi. L. Rev., Vol. 45, No. 1 (Fall 1977).

3/ Manufacturers might extract some of the profits of wholesaler collusion by raising wholesale prices, charging franchise or other fees, or imposing new obligations on wholesalers.

several manufacturers may appoint the same exclusive-territory wholesaler; and enforcement authorities may find wholesaler collusion more difficult to detect than manufacturer collusion, because wholesaler collusion would probably take place on a more localized scale.

In many, if not most, industries, the structural characteristics of production and distribution significantly reduce the likelihood that exclusive territories will or can be used to generate anticompetitive results in the manner discussed above. For example, if wholesaler concentration remains low, even with widespread use of exclusive territories, the likelihood of effective collusion at that level also remains low. Even in those situations where common use of exclusive territories creates high wholesaler concentration, the likelihood of successful collusion at that level is reduced if manufacturer concentration is low, 4/ or entry into manufacturing is easy. If the latter conditions prevail, some manufacturer--an established firm or a new entrant--would be strongly encouraged to exploit the opportunity for new sales created by the high prices and restricted availability of other manufacturers' products resulting from the wholesaler collusion. The distribution of such manufacturer's product may be accomplished by the manufacturer's creation of its own distributors (downstream vertical integration), by luring existing distributors away from the collusive scheme, or by inducing the entry of new distributors.

Unfortunately, none of the above mitigating factors is present in the beer industry. Indeed, this industry appears to be one in which the risk that widespread use of exclusive territories may produce anticompetitive effects is almost uniquely high.

Regarding concentration, in 1980 the top two brewers had a combined national market share of 50.0 percent and the top four had 67.1 percent. 5/ Brewer concentration at the state level was often significantly higher than national concentration. For example, in 1980, the four-firm sales concentration ratio exceeded 80 percent in 30 of 39 states for

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4/ Low concentration in manufacturing is consistent with high concentration in wholesaling if several manufacturers appoint the same wholesaler to be their sole distributor in a given territory.

5/ 1981 Modern Brewery Age Blue Book.

which information was publicly available. 6/ The distribution system in the malt beverage industry translates high brewer concentration into high concentration at the wholesale level. We understand that virtually all brewers use exclusive territorial arrangements. Moreover, in many markets, different brewers utilize the same wholesaler. These factors result in concentration at the wholesale level that may exceed that at the brewer level. 7/ Further, a prospective entrant into brewing may encounter difficulties in establishing distribution channels. This is primarily due to state regulation that usually prohibits vertical integration by brewers into wholesaling, and places licensing requirements on entry by independent wholesalers.

For these reasons, we believe that exclusive territories may raise competitive concerns in the beer industry. We wish to preserve the option of challenging exclusive territories where they facilitate collusion, whether in the beer or any other industry, while recognizing that in most cases territories serve desirable purposes. The present law gives us this flexibility while the proposed legislation, we fear, does not.

At present, the legality of exclusive territorial arrangements is determined under Section 1 of the Sherman Act, 15 U.S.C. section 1. 8/ In applying Section 1 to such arrangements between suppliers and their distributors, courts utilize the "rule of reason" to ascertain whether, under all the circumstances, the particular arrangement is an unreasonable restraint of trade. Continental TV, Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977). This flexible approach

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6/ The breakdown was as follows: In six states, the four-firm concentration ratio exceeded 90 percent, in 30 states it exceeded 80 percent and in 39 states it exceeded 70 percent. The identity of the four leading firms differed in some states. *See* Steinman's Beer Statistics News, April 1981.

7/ While multiple brewer use of the same wholesaler would make concentration higher than at the brewer level, a possibly offsetting factor is that territories awarded by different brewers may not overlap perfectly, increasing perhaps the number of wholesalers in any geographic market. In any event, wholesale concentration is high.

8/ The first sentence of Section 1 of the Sherman Act, 15 U.S.C. § 1, states: "Every contract, combination . . . or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, is declared to be illegal."

reflects a correct judicial recognition of the fact that such arrangements, while not necessarily or even typically anticompetitive, may have anticompetitive effects, and may therefore require condemnation under Section 1, in certain circumstances.

Because of the differences in language between Sherman Act Section 1 and S. 1215, a court might find that exclusive territorial arrangements were lawful under S. 1215 even where it would conclude that they unreasonably restrained competition under the rule of reason. Under the language of S. 1215, exclusive territorial arrangements would be deemed lawful so long as the product was in "substantial and effective competition" with other malt beverages within a defined geographic area. However, the term "substantial and effective competition" is not defined in the bill, and its meaning is unclear. In addition, it is not clear which party would have the burden of establishing the presence or lack of such competition, how it is to be measured, or how much "substantial and effective competition" is necessary in order to satisfy the requirements of the bill if significant anticompetitive effects were to be shown.

We understand that Section 3 is intended to make clear that Section 2 of the bill is not to be interpreted as authorizing actual restraints of trade among competitors. We do not read Section 2 as permitting such a result, and we recognize that the antitrust laws would potentially be available to challenge actual collusion among competitors even if S. 1215 were enacted. However, it may be difficult to detect collusion at the wholesale level, especially where the number of firms in any geographic market is small or where they operate in localized markets. By the same token, there would also be difficulties in proving collusion, even where it exists. Such difficulties could largely be avoided if the flexibility of the present rule of reason approach were retained. The fact that we could proceed against actual collusion where it is detected does not negate the need for flexibility to be able to challenge exclusive territorial arrangements in those circumstances where they act to facilitate collusion and thereby pose a significant threat to consumer welfare.

Our opposition to S. 1215 is not lessened by Section 3, which states that nothing in the bill shall be construed to legalize "enforcement" of exclusive territorial arrangements by means of "price-fixing agreements, horizontal restraints of trade, or group boycotts" that would otherwise be unlawful. It is not the means of enforcement of such vertical arrangements that gives rise to our concern; it is the danger of collusion by wholesalers, facilitated by exclusive territorial arrangements.

Proponents of S. 1215 argue that it is necessary to "clarify" the law as to exclusive territorial arrangements in order to secure the economic benefits that such arrangements provide. However, brewers at present can and do enter into exclusive territorial arrangements with their wholesalers. The Supreme Court has expressly recognized that such arrangements may have beneficial effects, and has held that such arrangements are not unlawful unless they have unreasonable anticompetitive effects. Continental TV, Inc. v. GTE Sylvania, supra, at 58-59. Moreover, cases decided since GTE Sylvania have recognized the economic benefits that vertical territorial arrangements may provide. 9/ The present Administration has repeatedly declared its intention to avoid simplistic attacks on such arrangements where their procompetitive utility outweighs such anticompetitive risks as they might contain. Indeed, the Antitrust Division has publicly expressed its willingness to explain the utility of vertical arrangements to courts who must interpret Section 1 in private treble damage actions.

Proponents of S. 1215 cite only Norman Williams Co. v. Rice, 1980-2 Trade Cas. ¶ 63,484 (Cal. Ct. App.), cert.

9/ At least one appellate court has expressly recognized such benefits with respect to the malt beverage industry. In Del Rio Distributing, Inc. v. Adolph Coors Co., 589 F.2d 176 (5th Cir.), cert. denied, 444 U.S. 840 (1979), the Fifth Circuit Court of Appeals upheld a jury verdict that Coors' exclusive territorial restrictions were reasonable because there was ample evidence showing that the territories "were essential to maintaining quality control and service in the retail market" and resulted in "a long-term effect of making each distributorship stronger, better able to compete with other brands and provide better service." 589 F.2d at 179. For additional post-GTE Sylvania cases recognizing the beneficial effects of vertical territorial arrangements, see, e.g., Donald B. Rice Tire Co. v. Michelin Tire Corp., 638 F.2d 15, 16 (4th Cir. 1981), cert. denied, BNA Antitrust & Trade Reg. Rep. No. 1034, at A-2 (Oct. 8, 1981); Cowley v. Braden Industries, Inc., 613 F.2d 751, 755 (9th Cir. 1980), cert. denied, 446 U.S. 965 (1980); Abadir & Co. v. First Mississippi Corp., 1981-2 Trade Cas. ¶ 64,180 (5th Cir.); Mesirow v. Pepperidge Farm, Inc., 1981-2 Trade Cas. ¶ 64,292 (N.D. Cal.); Continental T.V., Inc. v. GTE Sylvania, Inc., 461 F. Supp. 1046, 1052 (D. Cal. 1978); Newberry v. Washington Post Co., 438 F. Supp. 470, 475-76 (D.D.C. 1977).

granted, BNA Antitrust & Trade Reg. Rep. No. 1042, at A-1 (12-3-81), in support of their contention that applicability of the antitrust laws to exclusive territorial arrangements requires legislative clarification. We disagree that that case creates any real confusion as to, or that it undermines, GTE Sylvania's application of the rule of reason to exclusive territorial arrangements between a manufacturer and its customers. Norman Williams involved a challenge to a California statute which prohibited a licensed importer from importing distilled spirits into California unless he had been designated as an authorized importer by the brand owner. In effect, the California scheme provided a mechanism to enforce vertical territorial arrangements. Nevertheless, the court analyzed the conduct authorized by the statutory scheme under a per se test. The United States filed a brief as amicus curiae on a petition for a writ of certiorari to the United States Supreme Court urging reversal, among other things, on the ground that the California court had failed to recognize that the import restraints would have operated to preserve vertical territorial arrangements and, hence, should have been analyzed under the rule of reason. The Supreme Court has granted certiorari in that case. We are confident that the Supreme Court will correct the California Court's error, and that such judicial action is far preferable to enactment of S. 1215.

We therefore view the bill as an unwarranted exception to the antitrust standards applied to most other American businesses. The antitrust laws embody the fundamental national policy of free market competition. They are flexible and adaptable to a variety of factual circumstances in virtually any industry. As the January 1979 Report of the President's National Commission for the Review of Antitrust Laws and Procedures concluded, Congress' reliance upon the antitrust laws to protect and promote competition is abundantly justified, and exceptions from this general policy should only be made where there is "compelling evidence of the unworkability of competition or a clearly paramount social purpose." Id. at 177. No such showing has been made with respect to the malt beverage industry, and we believe none could be made.

Most important, to the extent that genuine clarification of the antitrust laws governing exclusive territories may be desirable, we believe that clarification should proceed on a general basis and not through special-interest legislation. Legitimization of exclusive territories in the beer industry may be undesirable not only in and of itself, it may also be construed to imply, incorrectly, that territories are less legitimate in industries not affected by this legislation.

We recognize that the Soft Drink Interbrand Competition Act ("Soft Drink Act" 15 U.S.C. §§ 3501-03), was enacted during the last Congress, and that that Act is similar to S. 1215. The Department of Justice objected repeatedly and strenuously to passage of that Act, among other reasons, for fear that it might be interpreted as creating a standard of legality for vertical territorial arrangements in the soft drink industry different from that contained in Section 1 of the Sherman Act. Indeed, it has been so interpreted by at least one court, 10/ and S. 1215 could be similarly interpreted.

Furthermore, introduction of S. 1215 confirms the validity of our repeatedly expressed fears that passage of the Soft Drink Act would create an undesirable precedent for similar special interest legislation applicable to other industries. Certainly, enactment of the Soft Drink Act does not justify creating another bad precedent. 11/ If Congress followed that precedent, it would cast further doubt on the universal applicability of the antitrust laws to the unregulated sectors of our economy and invite even further attempts by other industries to seek special interest legislation. Such a course could only lead to a patchwork of differing antitrust rules that would greatly complicate antitrust enforcement and deprive the antitrust laws of much of their utility. In recent years, Congress has increasingly narrowed existing antitrust immunities, and has relied more heavily upon competition, even in highly regulated industries. Such movement has been seen, for example, in the airline, trucking and rail industries and

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10/ Coca-Cola Co. v. FTC, 642 F.2d 1387 (D.C. Cir. 1981). There is some legislative history, however, not cited in Coca-Cola v. FTC, which supports the conclusion that no different standard of legality was created and that, instead, the standard of GTE Sylvania, *supra*, still applies. *See, e.g.*, H.R. Rep. No. 96-1118, 96th Cong., 2d Sess. 4-5, 16, 22, 24; 126 Cong. Rec. H 5534 (daily ed.) June 24, 1980. *But see* H.R. Rep. No. 916-1118, *supra*, at H 5536-37.

11/ We note that the Soft Drink Act was initially proposed in response to FTC proceedings against seven soft drink syrup manufacturers. When the FTC held, in 1978, that the territorial arrangements constituted unreasonable restraints of trade, the soft drink industry pressed its efforts to have that legislation enacted and argued that it was necessary to correct a misapplication of the rule of reason to vertical territorial arrangements as required by GTE Sylvania. That situation does not exist with regard to the malt beverage industry.

is presently occurring in the intercity bus, telecommunications and financial institutions industries. Establishment of an antitrust standard for the malt beverage industry potentially different from that applicable to other industries would be inconsistent with this desirable trend.

Conclusion

In sum, the Department of Justice believes that enactment of S. 1215 would be unnecessary and unwise. The Department of Justice, the Supreme Court, and numerous lower courts have expressly recognized the benefits from exclusive territorial arrangements and the courts have repeatedly held that such arrangements are not unlawful unless they have unreasonable anticompetitive effects. S. 1215 might be held to legalize exclusive territorial arrangements even if they had substantial anticompetitive effects and would be held unlawful under proper application of the rule of reason.

There is simply no valid reason why this industry should not continue to be subject to the same flexible antitrust rules applicable to most other industries. Indeed, passage of S. 1215 would further erode the general applicability and utility of the antitrust laws.

Accordingly, the Department of Justice opposes enactment of S. 1215.

The Office of Management and Budget has advised that there is no objection to the submission of this report from the standpoint of the Administration's program.

Sincerely,

(Signed) Robert A. McConnell

Robert A. McConnell
Assistant Attorney General

United States Department of Justice
WASHINGTON, D.C. 20530

DEPUTY ASSISTANT ATTORNEY GENERAL
ANTITRUST DIVISION

18 NOV 1982

Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
Washington, D. C. 20510

Dear Mr. Chairman:

I have enclosed answers to the questions asked in your letter of July 2, 1982, and to the requests made by Senator Laxalt during my testimony of June 21, 1982, on S. 1215, the "Malt Beverage Interbrand Competition Act." I appreciate the opportunity to submit these responses for the record.

Sincerely yours,

Abbott B. Lipsky, Jr.
Deputy Assistant Attorney General
Antitrust Division

Enclosures

1. Questions Related to The Soft Drink Industry

Senator Laxalt asked for a comparison of the soft drink and malt beverage industries with respect to the possibility of horizontal collusion being facilitated by exclusive territorial arrangements. He also wanted to know what our experience has been with respect to collusion in the soft drink industry. (Hearing Transcript at 38-39.)

Because the likelihood of collusion among the firms competing in a market increases as the number of firms in the market is reduced to a very small number, a proper comparision of the possibility of collusion in the soft drink and malt beverage industries requires a comparison of the concentration figures for relevant geographic markets in the two industries. In the malt beverage industry, the top two brewers in 1980 reportedly had a combined national market share of 50.0 percent, and the top four firms reportedly had 67.1 percent. 1/ Corresponding reported national market shares for the soft drink industry are 58.7 percent for the top two firms and 68.5 percent for the top four firms in 1981. 2/ Thus, concentration at the manufacturing levels of the two industries is of similar, large magnitude.

For purposes of assessing the possibility of wholesaler collusion, however, what is relevant is concentration at the wholesaler level, where the collusion would occur. In this regard, the distribution system in both industries would appear to translate the high manufacturer concentrations into high wholesaler concentrations and, hence, high likelihoods of collusion in local geographic markets. This translation is due to the extensive use of exclusive territories in both industries and the fact that, in many markets, manufacturers use the same wholesaler. We are unable, however, to assess the degree of that translation precisely and, hence, the relative dangers of wholesaler collusion for the two industries. In order to do so, we would have to know for each geographic area involved, in each industry, the extent to which exclusive territories awarded by different manufacturers overlap and the extent to which different manufacturers

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1/ 1981 Modern Brewery Age Blue Book.

2/ Beverage World, May 1982. These reported soft drink market shares do not include the market shares of a few minor brands sold by Coca Cola Co., the number one firm, by Pepsi Cola Co., the number two firm, and by Dr. Pepper, the number three firm. The Federal Trade Commission may have more accurate market share data because the Commission, through an informal arrangement with us, has tended to take a leading role with respect to practices in the soft drink industry.

award an exclusive territory to the same wholesaler. This information should vary from market to market, and we have insufficient information to assess the relative dangers of wholesaler collusion in the two industries.

Senator Laxalt also inquired about our actual experience with collusion in the soft drink industry. Most investigations into this industry are performed by the Federal Trade Commission, pursuant to an informal working agreement with us. Nevertheless, we are at present exploring allegations of horizontal collusion in this industry in various parts of the country. Additionally, since 1970 we have opened and closed fourteen investigations of horizontal price fixing in this industry; no cases were brought in that time period, however.

Finally, let me stress that, even assuming high levels of concentration and collusive risks in the soft drink and malt beverage industries, we recognize the many beneficial uses of exclusive territorial arrangements in these and other industries. Because of these benefits, exclusive territorial arrangements usually are not anticompetitive and, hence, are not illegal under Section 1 of the Sherman Act. It is only in those rare instances where the arrangements facilitate horizontal collusion that they are anticompetitive and, hence, illegal under existing law. S. 1215, however, could have the unfortunate effect of validating such arrangements, even where their effect is on balance anticompetitive.

2. Questions Related to Rice v. Norman Williams

Senator Laxalt requested a recapitulation of the contentions made in Rice v. Norman Williams so that the Committee will know what was before the Supreme Court in that case. He also asked whether S. 1215, if enacted, would have any impact on that case. (Hearing Transcript at 31.)

In response to Senator Laxalt's request for a recapitulation of contentions made in Norman Williams, I will summarize the judicial opinions and our brief filed therein. As I am sure you know, subsequent to my testimony the United States Supreme Court unanimously reversed the opinion of the California Court of Appeal in that case. See Rice v. Norman Williams, 1982-2 Trade Cas. ¶ 64816 (U.S. 1982).

At issue in Norman Williams was a California statute which prohibited a licensed importer from importing distilled spirits into California unless he had been designated as an authorized importer by the brand owner. Apparently, the statute was enacted to close the so-called "Oklahoma Connection," which was undermining the ability of distillers to establish exclusive vertical territories in California. Prior to enactment of the California statute, Oklahoma's statutes were understood to require any distiller or brand owner selling its products to Oklahoma wholesalers to sell to all wholesalers on a nondiscriminatory basis. Oklahoma law further authorized such wholesalers to sell to any "qualified persons" out of state. These provisions apparently were understood to bar a distiller or brand owner who wished to sell to Oklahoma wholesalers from insisting that the wholesalers decline to sell to persons who wished to import the liquor into California without authorization from the distiller or brand owner. Therefore, licensed importers in California who were not authorized by a brand owner to deal in its brand were nevertheless able to obtain supplies through Oklahoma suppliers.

The California Court of Appeal held that the California statute was invalid on its face, believing that it conflicted with Section 1 of the Sherman Act. Norman Williams v. Rice, 1980-2 Trade Cas. ¶ 63,484 (Cal. Ct. App. 1980). The premise of the holding was that the conduct of a brand owner acting pursuant to the statute, in effect preventing an undesignated California importer from purchasing distilled spirits from an independent Oklahoma wholesaler, would constitute a per se violation of Section 1 of the Sherman Act. The court rejected the contention that the case was controlled by Continental T.V. Inc. v. GTE Sylvania Inc., 433 U.S. 36 (1977), which held that vertical territorial restraints should be judged under the rule of reason rather than a per se rule of illegality. GTE, reasoned the California court, involved only "a manufacturer's chosen method of product distribution enforced by a refusal to sell to retailers outside of their assigned territories," whereas the instant case did not involve an attack by the wholesalers on the brand owner's refusal to trade with them. ¶ 63,484 at 76536. Rather, the wholesalers "attacked the state provided authority of the distillers to prohibit them from trading with others" and "[n]othing in [GTE] authorizes a state to delegate such power to a private party." Id. 3/

After the California court's decision, a petition for writ of certiorari to the California court was filed in the Supreme Court of the United States. At the request of the Supreme Court, the Department of Justice filed a brief as amicus curiae, a copy of which is enclosed. The brief concluded that the California

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3/ The court also held that the California statute is not protected by the state action doctrine of Parker v. Brown, 317 U.S. 341 (1943), and that the Twenty-first Amendment does not shield the California statute from preemption by the Sherman Act.

court was incorrect in holding that the California statute impermissibly conflicted with the Sherman Act. Initially, the brief argued that the California statute does not require a brand owner to impose a vertical restraint on a wholesaler--it merely enables him to do so, if he so chooses, by eliminating the effect of the "Oklahoma Connection." Because the statute does not require a brand owner to impose vertical restraints of a kind that may violate the Sherman Act, the fact that a particular brand owner might abuse its powers in imposing such restraints (and might rely on the California statute to police them) is not a basis for invalidating the statute on its face. Next, the brief argued that the California court erred in holding that the California statute is in conflict with the Sherman Act insofar as it enables a brand owner to prevent a nondesignated importer from purchasing the product from an Oklahoma wholesaler. The court's holding in this regard was based on its conclusion that this conduct by a brand owner would constitute a per se violation of the Sherman Act, which conclusion is incorrect in view of the Supreme Court's holding in GTE Sylvania.

As previously stated, the Supreme Court recently reversed the decision of the California Court of Appeal in Norman Williams. The Court, applying a preemption analysis to the California statute at issue, decided that there was no irreconcilable conflict between the federal and state regulatory schemes involved. A state statute, reasoned the Court, can be preempted prior to enforcement only if the statute on its face irreconcilably conflicts with federal antitrust policy. This can occur only if the statute requires or authorizes conduct that necessarily constitutes an antitrust violation in all instances, or if it places irresistible pressure on a private party to violate the antitrust laws in order to comply with the statute. Such preemption can occur under Section 1 of the Sherman Act only when the conduct contemplated by the statute is in all cases a per se violation--not when it is to be analyzed under the rule of reason. The California statute in Norman Williams, reasoned the Court, merely enforces the distiller's decision to distribute its goods through vertical exclusive territories, a practice the Court held in GTE Sylvania to be judged by the rule of reason. Moreover, the statute does not require the distiller to use exclusive territories--that is up to the distiller. It is irrelevant, stated the Court, that the distiller's ability to restrict intrabrand competition in this manner had the imprimatur of a state statute. The California statute merely restored what Oklahoma law had taken away: the distiller's ability to determine which wholesalers may import its products into California. The distiller's actions under the California statute are therefore subject to analysis under the rule of reason and, hence, there is no basis to invalidate the statute on its face by force of the Sherman Act. 4/

Senator Laxalt asked whether S. 1215 would have any impact on the California court's decision in Norman Williams. This question now seems moot in light of the Supreme Court's reversal of the California court's decision. However, even if the Supreme Court had not reversed the California court, it does not appear, for two reasons, that S. 1215 would have changed the result of that case. First, the statute at issue in Norman Williams relates to distilled spirits, not malt beverages, whereas S. 1215 relates only to malt beverages. Second, even if Norman Williams had involved malt beverages, the solution offered by S. 1215 does not address the error made by the California court. Section 2 of S. 1215 is an apparent attempt to prevent misapplication of the present rule of reason, when assessing exclusive territories in the malt beverage industry, by replacing the language of Section 1 of the Sherman Act with new language applicable to exclusive territorial agreements in that industry. The error of the California court, however, was not in its misapplication of the rule of reason; it was in its mischaracterization of the conduct at issue as conduct different from the private use of exclusive territories and in its failure to evaluate that conduct under the rule of reason. Hence, even if Section 2 of S. 1215 had been the prevailing antitrust standard for analyzing the legality of exclusive territorial arrangements at the time of the California court's decision (and that decision had involved malt beverage products instead of distilled spirits), there is no reason to believe that the California court would not have made the same mistake in characterizing the conduct and thus reached the same result.

3. Amending S. 1215

> Senator Laxalt asked for any constructive suggestions involving the wording of the bill in the event the Senate decides to endorse its substantive concept (Hearing Transcript at 39.)

As stated during my testimony, one of our primary difficulties with the bill is its articulation of new language as the antitrust standard for the legality of exclusive territories in the malt beverage industry. Such new language would undoubtedly undergo extensive judicial interpretation, a highly undesirable result in view of the fact that judicial interpretation of the Sherman Act--87 years after enactment--reached a satisfactory approach to non-price vertical restraints in GTE Sylvania. The basic statute governing

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4/ Consequently, reasoned the Court, there is no need to decide whether the statute may be saved from invalidation under the "state action" doctrine or under the Twenty-first Amendment.

the antitrust legality of exclusive territories--Section 1 of the Sherman Act--is entirely satisfactory. The basic approach to judging the competitive effects of the practice under Section 1--the rule of reason approach adopted in GTE Sylvania, which recognizes the strong pro-competitive potential of vertical contractual relationships--is entirely satisfactory. We would suggest no amendment because no change in current law is warranted in these respects.

I would again like to emphasize our belief that new legislation is not needed to enable the malt beverage or any other industry to realize the benefits of exclusive territorial arrangements. That is because these arrangements, except for those few instances where they are anticompetitive, are not illegal under present law. However, if Congress finds that judicial application of the rule of reason to exclusive territories is at present confusing, and that legislative clarification is needed, we believe that such clarification should proceed on a general basis, not through special interest legislation. We would be happy to work with the Committee in devising the exact language to be used in any such general legislation. So-called legislative "legitimization" of exclusive territories in only the malt beverage industry is undesirable not only in and of itself, but also because it might be construed to imply--quite incorrectly-that such arrangements are less legitimate in industries not affected by this legislation. Enactment of such special interest legislation would also cast further doubt on the applicability of the antitrust laws to other sectors of our economy and may invite other industries to seek similar legislation.

4. Additional Questions asked By Chairman Thurmond

   a. In your prepared statement you assert that "virtually all brewers use exclusive territorial arrangements . . . ." If that is so, how much practical impact on competition do you expect S. 1215 could have?

Although we are unable to quantify precisely the potential impact of S. 1215, we believe the structural and regulatory characteristics of the malt beverage industry render it almost uniquely susceptible to the anticompetitive effects of legislation of this nature. These effects could be substantial. While exclusive territorial arrangements are usually procompetitive, efficiency-enhancing practices which are not illegal under the Sherman Act, these arrangements could facilitate wholesaler collusion in particular circumstances, and the Sherman Act provides the flexibility to challenge them in such circumstances. If S. 1215 is judicially interpreted as creating a weaker standard than that of the Sherman Act, it might legalize exclusive territories that are in fact anticompetitive. The harmful economic consequences might be both substantial and difficult to remedy.

b. Given all of the factors about the malt beverage industry from which you conclude that exclusive territories may raise competitive concerns, might it be possible for the Department of Justice to challenge state laws which permit such arrangements?

The Supreme Court held in *Rice v. Norman Williams* that a state statute may be preempted on its face by the antitrust laws only if the conduct that it mandates or authorizes is in all cases a violation of those laws. If the activity addressed by the statute may be legal under some circumstances the statute may not be preempted in the abstract; rather, the state law may be preempted only where its application to a specific set of facts creates a conflict with federal law.

Because exclusive territorial arrangements are judged under the rule of reason, a state statute that permits these arrangements cannot--under *Rice v. Williams*--be held invalid on its face under a theory of preemption by the Sherman Act. Moreover, since these arrangements will almost always be procompetitive, it would be counterproductive to invalidate a statute which requires or permits them merely because in a few instances they may be anticompetitive. In those few situations where the exclusive territorial arrangements facilitate horizontal collusion, and are not immunized by the state action doctrine of *Parker v. Brown*, 317 U.S. 341 (1943), 5/ they would be illegal under Section 1 of the Sherman Act and the state statute would be preempted.

c. We will hear testimony from the brewers to the effect that because of governmental restrictions on price promotions, discounts, multi-brand marketing, and advertising, a free market for malt beverages does not exist. They argue that these restrictions make it difficult for them to market their product, creating a need to encourage their wholesaler's marketing efforts through exclusive territories. How do these factors impact on your analysis?

As a strong proponent of free market competition and an opponent of unnecessary government regulation, the Department is sympathetic to the brewers' concerns over extensive state regulation. However, the existence of such regulation does not alter our basic view that, while exclusive territories usually serve legitimate procompetitive purposes, in exceptional circumstances they can be anticompetitive. Indeed, as I pointed out in my testimony, state regulation of this industry actually increases

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5/ *See* note 6, *infra*.

the risk of collusion and, hence, antitrust illegality, in two ways. First, state regulation often prohibits vertical integration by brewers into wholesaling, and can otherwise erect barriers to entry by independent wholesalers. By controlling the number of wholesalers in this manner, the threat of new entry is reduced, thus enhancing the risk of collusion. Second, state regulation often compels advance public announcement of prices and adherence to those prices, thereby facilitating price collusion and providing the means by which it may be monitored and policed.

d. Do you believe that there is any confusion as to the state of the law regarding exclusive territories for the malt beverage industry under the purview of state legislation? Is S. 1215 necessary to permit states to pass laws allowing exclusive territories?

As stated in my testimony, I do not believe that there is significant confusion regarding the federal antitrust legality of exclusive territorial arrangements. In Valley Liquors, Inc. v. Renfield Importers Ltd., 678 F.2d 742 (7th Cir. 1982), for example, Judge Posner clearly recognized that the legality of a distribution arrangement between a supplier of wines and liquors and its exclusive wholesale distributors is subject to the rule of reason, and that the arrangement would not unreasonably restrain trade unless, "weighing effects on both intrabrand and interbrand competition, it made consumers worse off."

The fact that a particular exclusive territorial arrangement is under the purview of state law does not, in our view, add confusion to assessing the legality of that arrangement. The relevance of state regulation to the arrangement's legality is twofold. First, as stated in response to the previous question, state regulation can increase the risk of collusion and, hence, of antitrust illegality. Second, the fact of state regulation is relevant in determining whether the arrangements are immunized by the state action doctrine of Parker v. Brown, 317 U.S. 341 (1943). 6/ While both of these factors are to be considered in determining the legality of a particular arrangement, we do not believe they make the determination confusing.

6/ Under that doctrine, we believe it is clear that where the defendant is a private party, the private conduct is exempted from antitrust scrutiny only if the restrictive conduct was "compelled" by governmental action. See, e.g., Cantor v. Detroit Edison Co., 428 U.S. 579 (1976); Goldfarb v. Virginia State Bar, 421 U.S. 773 (1975). If the restraint is viewed as emanating from a governmental entity, the entity's action must be pursuant

Finally, we do not believe that S. 1215 is necessary to permit states to pass laws allowing exclusive territories. As indicated in response to question 4.b., supra, under the Supreme Court's decision in Norman Williams, a state can at present pass such a law and the law will not be declared invalid on its face.

e. Do you believe that the existence of the federal antitrust law regarding exclusive territories is in any way restrictive of the right of states to regulate alcoholic beverages under the 21st Amendment to the Constitution?

To the extent that a state statute is invalid on its face or in particular situations because it conflicts with Section 1 of the Sherman Act, federal antitrust law would indeed be restrictive of a state's ability to regulate alcohol. This conflict between a state's ability to regulate alcohol and the antitrust laws was recently discussed in California Retail Liquor Dealers Assn. v. Midcal Aluminum, Inc., 445 U.S. 97 (1980). There, the Court held that a state-imposed resale price maintenance scheme was invalid in light of Section 1 of the Sherman Act, notwithstanding the Twenty-first Amendment. The Court specifically concluded that Section 2 of the Twenty-first Amendment does not permit California unfettered discretion to countermand the congressional antitrust policy--adopted under the commerce power--in favor of competition. 7/

Early Supreme Court decisions, stated the Midcal Court, "resisted the contention that Section 2 freed the states from all restrictions upon the police power to be found in other provisions of the Constitution." 445 U.S. at 108. Subsequent decisions, while giving "wide lattitude to state liquor regulation, also stressed that important federal interests in liquor matters survived the ratification of the Twenty-first Amendment." Id. One such

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6/ (FOOTNOTE CONTD) to a clearly articulated state policy to replace competition with regulation, and there must be active governmental supervision of the restrictive practice in order to prevent abuses that would arise due to the absence of competition in the regulated sector. See, e.g., Community Communications Co. v. City of Boulder, 102 S. Ct. 835 (1982); California Retail Liquor Dealers Ass'n. v. Midcal Aluminum Inc., 445 U.S. 97 (1980); City of Lafayette v. Louisiana Power & Light Co., 435 U.S. 389 (1978).

7/ U.S. Const. amend. XXI, § 2 states that "The transportation or importation into any State, Territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited."

federal interest involves the congressional interstate commerce power, pursuant to which the antitrust laws were enacted. Quoting Hostetler v. Idlewild Liquor Corp., 377 U.S. 324, 331-332 (1964), the Midcal Court stated:

> [T]o draw a conclusion . . . that the Twenty-first Amendment has somehow operated to repeal the Commerce Clause wherever regulation of intoxicating liquor is concerned would, however, be an absurd oversimplification. If the Commerce Clause had been pro tanto 'repealed,' then Congress would be left with no regulatory power over interstate or foreign commerce in intoxicating liquor. Such a conclusion would be patently bizarre and is demonstrably incorrect.

Id. at 109. Again quoting Hostetler, the Midcal Court noted that "[b]oth the Twenty-first Amendment and the Commerce Clause are parts of the same Constitution," and, "like other provisions of the Constitution, each must be considered in the light of the other, and in the context of the issues and interests at stake in any concrete case." Id. With specific reference to federal antitrust law, the Court "acknowledged the importance of the Act's procompetition policy" and the fact that Congress "exercise[d] all the power it possessed" under the Commerce Clause when it approved the Sherman Act. Id. at 111. The Court then weighed the asserted state interests involved with "the national policy in favor of competition," concluded that the state interests "are less substantial" than the national policy, and enjoined the state's resale price maintenance scheme.

Applying the Midcal analysis to a state statute that authorizes or facilitates, but does not compel, exclusive territorial arrangements, we have considerable doubt that a vertical restraint imposed by an individual distiller and enforced through the state statute, if anticompetitive and, hence, in violation of the Sherman Act in a particular situation, would be sufficiently supported by legitimate state interests to be sustained under the Twenty-first Amendment in that situation. We stress again, however, that any such conflict between the Twenty-first Amendment and the Sherman Act will be rare, since exclusive territories are often procompetitive and, hence, legal under the Sherman Act.

g. How much of a barrier to entry do state licensing requirements create in practice?

Various state regulations (e.g., regulations on labeling and advertising, imposition of license fees) can make it more difficult and costly to do business, thereby making it less attractive for firms to enter the industry as wholesalers. Furthermore, state regulations often prevent a wholesaler from coming into the market altogether. In this regard, some states prohibit brewers from integrating downstream into a wholesaling function, and some states require that only one wholesaler sell a particular brand in a particular area.

Senator LAXALT. We will proceed now with a panel composed of Seymour Podolsky, who is with the National Beer Wholesalers' Association of America, from Southgate, Mich.; Lewis T. Nunnellee, Coastal Beverage Co., Inc., Wilmington, N.C.; and Edison R. Lara, Westside Distributing, Los Angeles, Calif.

Gentlemen, we welcome you to the committee. We look forward to your testimony. Proceed in any fashion that you would like.

STATEMENTS OF A PANEL CONSISTING OF SEYMOUR PODOLSKY, BEVERAGE DISTRIBUTING CO., SOUTHGATE, MICH.; LEWIS T. NUNNELEE, COASTAL BEVERAGE CO., INC., WILMINGTON, N.C.; AND EDISON R. LARA, WESTSIDE DISTRIBUTING, LOS ANGELES, CALIF.

Mr. PODOLSKY. Mr. Chairman, thank you very much.

My name is Seymour Podolsky. I am a graduate of the Harvard University Law School, a member of the bar of the State of Michigan. After several years of full-time practice of law, I joined my family-owned beer distributorship in the town of Southgate, Mich., handling primarily the products of the Stroh Brewing Co.

The business was established by my father in 1920. It survived Prohibition with nonalcoholic products, soft drinks, and was one of the first licensees in Michigan after repeal in 1933. I have been active in the business for over 30 years. Currently, my brother and I conduct the business together. Our business employs 26 people, owns 19 trucks, has a 17,000-square-foot warehouse, and distributes 600,000 cases of malt beverages annually to approximately 1,100 retail outlets.

I am here today to present to you the views of all of the members of the National Beer Wholesalers' Association of America, Inc., and all of the State beer wholesalers' associations. Our membership represents over 3,000 small business distribution centers handling about 90 percent of the beer sold in the United States. These businesses average about the same size as mine does. Wholesalers also act as agents for State tax collections of well over $1 billion annually and employ an estimated 80,000 people. On behalf of all these people, we want to thank you for this opportunity to present our views.

With me today are two other beer wholesalers. To my right is Ed Lara of California; to my left, Lew Nunnelee of North Carolina. They will each make a short statement at the conclusion of my formal testimony.

I also want to submit for the record a document entitled Legal Response to Arguments by Objectors to S. 1215.

Senator LAXALT. Without objection, it will be so ordered.

[Material referred to follows:]

LEGAL RESPONSE TO
ARGUMENTS BY OBJECTORS
TO S.1215

June 20, 1982

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I. Summary Of The Legal Need For S.1215

I. The Structure of the Brewing, Beer Distribution and Retailing System Demonstrates the Need for the Act.

In Continental TV, Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977), the Court overruled its earlier decision in United States v. Arnold Schwinn & Co., 388 U.S. 365 (1977), by holding that vertical territorial restrictions entered into by distributors and manufacturers are not per se violations of the Sherman Act. Rather, the Court ruled, such arrangements are to be tested on a case-by-case basis under the "Rule of Reason" to determine whether, in the circumstances of a particular case, the goal of competition is fostered or impeded. In so holding, the Court recognized that competition often is most effectively fostered by vigorous interbrand product competition. It acknowledged that, in certain circumstances, interbrand competition is best promoted by permitting manufacturers and wholesalers to enter into vertical agreements to provide protection for the distributor.

The Court was specific in identifying several circumstances in which such vertical arrangements, have procompetitive effects. For example, new manufacturers and manufacturers entering new marketing areas may have to give wholesalers exclusive territorial areas in order to encourage the wholesalers to risk essential investments of capital and the employment of labor. 433 U.S. at 55. Similarly, established manufacturers often need such arrangements in order to encourage their wholesalers to engage in adequate promotional activities, to provide proper servicing of retailers, and to assure appropriate quality control in the interest of consumers. Id. Because of the problems of "free riders" and other "market imperfections," the Court recognized that such services may not be provided by wholesalers unless they are given suitable territorial protection. Id. Further, the Court noted that manufacturers have, in any event, an economic interest in maintaining as much interbrand competition as is consistent with the efficient distribution of products. Id. at 56.

The economic structure of the malt beverage brewing, wholesaling and retailing industries demonstrates that all the considerations that led the Court to abolish the *per se* rule against vertical territorial allocation are fully applicable to the wholesaling of malt beverages. Indeed, the structure of the industry makes it clear that competition could be fostered most effectively through federal legalization of vertical territorial restrictions by the Malt Beverage Interbrand Competition Act.

In both the case of the brewer and the retailer, there has been increasing concentration even within the past five years. Thus, while in 1975 the top five brewers produced 66% of total beer sold in this country, in 1980 that figure was almost 75%. Similarly, with respect to retailers, the ten leading publicly held nationwide supermarket chains represented 65% of that category's sales in 1975, while in 1980 that figure had risen to 70%.

Standing between these two highly concentrated elements of the malt beverage distribution system is the beer wholesaler or "distributor." He is usually a small businessman. In 1978 (the most recent information available by size) almost 27% of the nation's wholesalers employed between 1 and 4, while 80% of beer wholesalers have less than 50 employees.

Because of this relatively low concentration, the distributor has been the most effective force in promoting interbrand competition in the malt beverage market in the United States. That competition has worked directly in the interest of consumers. While soft drink prices have increased by 195% since 1965, wine by 114%, whiskey by 38%, coffee by 298%, non-alcoholic beverages by 290%, and all items in the Bureau of Labor Statistics Price Index have increased by 161%, beer prices have risen only 94%.

Given the vital role and small size of the distributor, all of the considerations that led the Supreme Court to abolish the per se rule against vertical territorial restrictions in GTE Sylvania, supra, are present in the malt beverage wholesaling industry. Due to the high level of interbrand competition among wholesalers, they must be prepared to make relatively large investments of capital and labor. Warehousing facilities, trucks, labor and other costs provide heavy burdens for relatively small local wholesaling firms. If a wholesaler is to risk such substantial investments in a business in which interbrand competition is intense, he must first be assured that the availability of a reasonable local marketing area, in which he will enjoy protection against intrabrand competition. Without such protection, wholesalers cannot be expected to risk the efforts and investments necessary to perform their important economic functions, and brewers cannot be assured that fresh beverages will be efficiently and economically distributed to retailers. Moreover, consumers could not be assured that wholesalers would have the incentive or the ability to provide reasonable levels of quality control.

In sum, application of the analysis of GTE Sylvania to the malt beverage brewing and distribution industries demonstrates that vertical territorial restrictions are necessary to foster vigorous competition. However, GTE

Sylvania did not immunize such arrangements from antitrust attack, and the concomitant expense and risk. See pp. 5-8, infra. The Malt Beverage Interbrand Competition Act, on the other hand, would allow brewers and wholesalers to enter into these pro-competitive arrangements safely. It is important to emphasize that this is all it will do. It will not remove truly anti-competitive agreements or practices from the reach of the law.

II. The Act Will Not Immunize Anti-Competitive Activities in the Malt Beverage Industry From the Antitrust Laws.

The language of the Malt Beverage Interbrand Competition Act itself makes it clear that the industry will remain fully subject to the antitrust laws, outside the narrow area of pro-competitive vertical territorial protection. Section III of the bill states that:

> "Nothing in this Act shall be construed to legalize the enforcement of provisions described in Section II of this Act [which legalizes vertical territorial protection where malt beverage product competition is 'substantial and effective'] in any written contract described in that Section by means of price fixing agreements, horizontal restraints of trade, or group boycotts, if such agreement, restraints, or boycotts would otherwise be unlawful."

The plain language of the Act should silence those who would characterize its narrow provisions as an "antitrust exemption."

III. The Act is Necessary to Protect the Malt Beverage Wholesaler Against the Extreme Costs and Risks of Antitrust Litigation.

While GTE Sylvania held that non-price vertical arrangements were not *per se* illegal under the Sherman Act, it did not immunize such arrangements from attack. Rather it held that the validity of such restrictions was to be tested under the "Rule of Reason," in which the Court considered the circumstances of a specific case to determine whether the restriction in question is reasonable. *Id.*, 433 U.S. at 59.

Thus, beer distributors may not rest easy because the Supreme Court has recognized that vertical territorial restrictions have pro-competitive effects in markets such as theirs. Nor are they protected by the various state laws that expressly make permissible such arrangements in the beer industry. Rather, the lure of treble damages and the potential for "Rule of Reason" litigation can be expected to result in numerous antitrust challenges. Moreover, malt beverage distributors may be subjected to serious financial burdens associated with such challenges regardless of whether they have merit under existing laws.

Thus, whenever litigation is commenced regarding the "reasonableness" of a vertical territorial restriction, it is inevitably lengthy, burdensome, and expensive. Such litigation requires a detailed examination of the specific conditions and circumstances of each of the particular local markets involved. Elaborate discovery and the presentation of expert economic testimony are virtually unavoidable. Even where, as in the cases involving the distribution of malt beverages, the ultimate reasonableness of the vertical arrangement appears clear from the outset, a court cannot be expected to resolve the issue without long proceedings and often a lengthy trial.

This threat of litigation is further increased by the lack of clarity of the law in this area. The GTE Sylvania rule has been interpreted and applied by the federal courts in a variety of the circumstances. Unfortunately the resulting caselaw presents inconsistent guidance in this area and provides little assurance that vertical non-price restrictions that promote competition will be safe from attack. Some of the numerous judicial attempts to interpret and apply GTE Sylvania are listed in the Appendix.

The murky nature of the caselaw means that these small business distributors not only must face the substantial costs of "Rule of Reason" litigation, but that they are also potentially subject to enormous treble damage awards. It is not uncommon for courts to assess substantial damages against distributors or other middlemen who cooperate in vertical non-price agreements. See, e.g., Venture Technology, Inc. v. Natural Fuel Gas Co., 1980-81 Trade Cases ¶ 63780

(W.D. N.Y. 1981) ($500,000); Engine Specialists, Inc. v. Bombardier, Ltd., No. 78-1492 (1st Cir. 1979) ($1,200,000); Mid-America ICE, Inc. v. John E. Mitchell Co., No. 69-654 (D. Ore. 1977) (over $700,000).

IV. Conclusion

The malt beverage wholesaler is a small businessman essential to the maintenance of vigorous interbrand competition in the malt beverage industry. He needs the protection associated with vertical territorial restrictions to justify the necessary investment to maintain that competition.

The Supreme Court has recognized the pro-competitive effects of vertical territorial restrictions under certain conditions. The malt beverage production and distribution system provides an almost classic example of such conditions. Yet beer wholesalers remain subject to antitrust attack precisely because they choose to enter into such pro-competitive arrangements.

Even where meritless, such antitrust litigation inevitably creates onerous burdens for defendants. Moreover, the confusion and lack of clarity that exists regarding the application of GTE Sylvania's "Rule of Reason" poses a threat of treble damages which could be crippling to many of these small businessmen. The passage of the Malt Beverage Interbrand Competition Act is necessary to clarify the law in this area, to allow pro-competitive vertical territorial restrictions, and to remove the costs associated with "Rule of Reason" antitrust litigation.

As demonstrated in Sections VI and VII of this memorandum, neither the objections of the Department of Justice nor of the Federal Trade Commission are relevant to the problems addressed by S.1215.

HAZARDS OF LITIGATION
RELYING UPON SYLVANIA

The federal courts frequently have applied and interpreted Continental TV, Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1976). The following list includes examples of such cases decided by each level of the federal courts. The approaches taken by these courts often have not been consistent.

1. McClatchy Newspapers v. Noble, 433 U.S. 904 (1977).

2. North American Soccer League v. National Football League, et al., Nos. 80-9153 (2d Cir. January 27, 1982) (Slip Op.).

3. United States v. Studiengesellschaft Kohle, M.B.H., No. 79-1634 (D.C. Cir. December 11, 1981) (Slip Op.).

4. Red Diamond Supply, Inc. v. Liquid Carbonic Corp., 637 F.2d 1001 (5th Cir. 1981).

5. United States of America v. Realty Multi-List, Inc., 629 F.2d 1351 (1980).

6. Consolidated Farmers Mutual Insurance Co. and Kansas Mutual Insurance Co. v. Anchor Savings Association, et al., No. 79-2260 (10th Cir. July 24, 1980) (Slip Op.).

7. Havoco of America, Ltd. v. Shell Oil Co., 626 F.2d 549 (1980).

8. Eiberger v. Sony Corporation of America, 622 F.2d 1068 (1980).

9. Catalano, Inc. v. Target Sales, Inc., 605 F.2d 1097 (1979).

10. United States of America v. Thomas J. Gillen, 599 F.2d 541 (1979).

11. Oreck Corp. v. Whirlpool Corp., 579 F.2d 126 (2d Cir. 1978).

12. *Columbia Metal Culvert Company, Inc.* v. *Kaiser Aluminum & Chemical Corporation*, 579 F.2d 20 (1978).

13. *Eastern Scientific Company* v. *Wild Heerbrugg Instruments, Inc.*, 572 F.2d 883 (1978).

14. *Oreck Corporation* v. *Whirlpool Corporation*, 563 F.2d 54 (1977).

15. *Balogh's of Coral Gables, Inc.* v. *Getz*, 510 F. Supp. 741 (1981).

16. *Venture Technology, Inc.* v. *National Fuel Gas Co.*, No. CIV-76-226 (W.D. N.Y. January 9, 1981) (Slip Op.).

17. *United States of America* v. *Quaker State Oil Refining Corporation*, Civil No. 56-69 (W.D. Pa. November 3, 1980) (Slip Op.).

18. *General Glass Co., Inc.* v. *Globe Glass and Trim Co.*, Nos. 71 C 921, *et al.* (N.D. Ill. June 26, 1980) (Slip Op.).

19. *Paralegal Institute, Inc.* v. *American Bar Association*, 475 F. Supp. 1123 (1979).

20. *Technical Learning Collective, Inc.* v. *Daimler-Benz Aktiengesellschaft and Mercedes-Benz*, No. K-77-1443 (D.C. Md. July 2, 1979) (Slip Op.).

21. *West Texas Utilities Co.* v. *Texas Electric Service Co.*, 470 F. Supp. 798 (N.D. Texas January 30, 1979) (Slip Op.).

22. *Southern Snack Foods, Inc.* v. *J & J Snack Foods Corporation*, 79 F.R.D. 678 (1978).

23. *La Preferida, Inc.* v. *La Victoria Foods*, No. 77 C 3926 (N.D. Ill. August 2, 1978) (Slip Op.).

24. *Krehl* v. *Baskin-Robbins Ice Cream Co.*, 78 F.R.D. 108 (1978).

25. *Lucas Hoist & Equipment Co.* v. *Eaton Corp.*, 76 F.R.D. 661 (1977).

Plaintiffs prevailed and received a money award in the following vertical (or partially vertical) cases:

1. Ohio-Sealy Mattress Manufacturing Co. v. Sealy, Inc., 1982-1 Trade Cas. (CCH) ¶ 64,507 (7th Cir. 1982) ($10,222,278).

2. Eiberger v. Sony Corp. of America, 1981-1 Trade Cas. (CCH) ¶ 63,963 (S.D.N.Y. 1981) ($81,290.05 plus attorneys' fees of $48,750.00).

3. Pitchford Scientific Instruments Corp. v. Pepi, Inc., 440 F. Supp. 1175 (D. Pa. 1977), aff'd without published opinion, 582 F.2d 1275 (3d Cir. 1978), cert. denied 440 U.S. 981 (1979) ($1,576,979.68, including attorneys' fees and costs).

Please note that the cited opinions are the most recent opinions found in each case, and usually are not the opinions in which liability was initially found.

II. S.1215 Is Not Special Interest Legislation

The opponents to the Bill rhetorically urge that this is special interest legislation.

It is not cogent to refer to a narrow, remedial clarification as a special interest proposal.

As Mr. Justice Powell observed, "antitrust deals with substance not form."

All antitrust questions depend upon economic reality. As to beer, the antitrust questions are complex and difficult because of the collision between the Twenty-First Amendment and the Sherman Act.

Under the Twenty-First Amendment each state has complete power to regulate the internal, intrastate distribution of alcoholic beverages. It can keep them out. It can tax them.

Most important here, each state licenses each brewer or importer, licenses each distributor and each retailer.

Each state can constitutionally determine who may engage in the business, where beer may be sold, and, of course, to which age groups any alcoholic beverage may be sold.

But as the Midcal case made clear, the federal antitrust laws can, where interstate competition is invaded, preempt what a state may do under the Twenty-First Amendment.

California Retail Liquor Dealers Association v. Midcal Aluminum, Inc., et al., 445 U.S. 97 (1980).

Consequently, that is the crux of what this Bill covers.

As pointed out, many states permit, and indeed some mandate, that exclusive territorially written agreements between a brewer and a wholesaler are legal under state law. That is recognition of the economic realities upon which this proposal is based.

But because of the existing confusion about the legality of those agreements under the Federal antitrust laws, this Bill is necessary to clarify the situation.

One does not solve that problem by simply using the rhetoric of calling this needed proposal "special interest legislation." Instead, the economic realities must be examined. As Justice Brandeis pointed out in the Chicago Board of Trade opinion: "the economic evil to be remedied must be balanced in the public interest against the narrow restraint that is sought."

III. What S.1215 Does And Does Not Do

S.1215's purpose is narrow and specific. It protects distributors and brewers against lengthy, burdensome and expensive private litigation challenging agreements creating distributional territories. In so doing, the bill recognizes that the Supreme Court has already held that such agreements are not *per se* illegal and that they may have important pro-competitive effects in markets such as malt beverages. The bill also takes account of the fact that many state laws expressly authorize such agreements in the beer industry. Based upon the pro-competitive effects of such agreements, already recognized by the Supreme Court and now conceded by the Department of Justice's comments on S.1215, the bill's primary result will be to prevent unnecessary private litigation, the heavy costs of which must ultimately be borne by consumers.

S.1215 does not create an antitrust "exemption." To the contrary, Section 3 of the bill expressly provides that the full panoply of antitrust enforcement devices will continue to be available against price-fixing, horizontal restraints of trade and group boycotts. The bill's only protection will be for pro-competitive vertical territorial agreements. As to every other issue and form of conduct, the law will be unchanged.

IV. Permitting "Free-Riders" In Distribution Is Anticompetitive And Not In The Public Interest

The economic evils of transshipment, what in antitrust law is called the "free-rider" problem in distribution, has long been recognized by courts and antitrust scholars as anticompetitive.

Wherever there is interbrand competition, and servicing by a distributor is necessary to protect consumers and product quality, paramountly in the case of a perishable product like beer, free-rider activities are demonstrably anticompetitive.

As Justice Powell pointed out in the *Sylvania* case, unless appropriate quality control in the interest of consumers can be provided by distributors, competition is destroyed by the free-rider.

To remedy that evil, territorial exclusivity agreements are widely used in distribution. Their pro-competitive "economic utility" is confirmed by many judicial decisions and extensive scholarly writings. *Continental T.V., Inc.* v. *GTE Sylvania, Inc.*, 433 U.S. 36, 55-56 (1977).

Professor, now Judge, Robert Bork termed this recognition of the clear ability of exclusive territorial distributor agreements, as "economic sophistication." He urged that it makes antitrust "a rational pro-consumer policy" in distribution.

Similarly, Judge Posner advanced the same conclusion in his treatise on Antitrust Law.

In an early 1942 decision, Judge Hand of the Second Circuit recognized the same concept (Boro Hall v. General Motors, 124 F.2d 822).

In another decision preceding Sylvania, Judge Ditter pointed out that where servicing to protect consumers is necessary, nonprice vertical restraints are in the public interest (Kaiser v. General Motors, 300 F. Supp. 33 (1975)).

Interbrand competition among malt beverages is indisputably vigorous. Beer brands are extensively advertised and promoted, and consumers enjoy the results of that rugged competition as to price, quality, and other characteristics.

At the same time, brewers can continue to compete effectively only if they can be assured that their wholesalers will distribute their products properly and efficiently.

Adequate measures of quality control are essential to guarantee the availability of fresh beer to consumers. Without such measures, a brewer's goodwill and the competitiveness of his products may be injured by stale or damaged beverages. Similarly, retailers must be served frequently and efficiently.

As clear on this record, in order to satisfy these obligations, wholesalers must make relatively large investments of capital and labor. Warehousing facilities, trucks, labor and other costs represent heavy burdens for relatively small local wholesaling firms.

If a wholesaler is to risk such substantial investment in a business in which interbrand competition is intense, he must first be assured the availability of a reasonable local marketing area in which he will enjoy protection against intrabrand competition.

Without such protection, wholesalers cannot be expected to risk the massive investment necessary to perform their important economic functions, and brewers cannot be assured that fresh beer will be efficiently and economically distributed to retailers.

As those economic factors make clear, exclusive territorial arrangements are imperative for the distribution of malt beverages.

Without such arrangements, both brewers and wholesalers who be stymied in their efforts to assure vigorous interbrand competition, and consumers would be denied the substantial advantages that such competition now affords.

Small local wholesaling businesses would be injured, and local employment and other significant benefits offered by those businesses would be adversely affected. Under the rule of reason principles established in Sylvania, exclusive territorial arrangements entered into between brewers and wholesalers should plainly be lawful.

V. Sylvania And The "Rule Of Reason" It Offers Does Not Solve The Wholesalers' Problem

Opponents of the Bill, particularly the Department of Justice and the Federal Trade Commission, suggest that the Sylvania decision of 1977 affords clear protection for beer wholesalers against the evils of "free-riders."

They admit that in the 1967 Schwinn decision, the Supreme Court tilted away from the rule of reason and held all nonprice vertical restraints *per se* illegal.

Of course, ten years later in Sylvania, the Supreme Court again tilted, and decided that territorial agreements could be examined by looking at all of the economic factors, at the existence of interbrand competition in the particular markets, and by balancing the interbrand competition against the loss of intrabrand competition occasioned by exclusive territorial arrangements.

No responsible antitrust lawyer could say that this affords any real protection to an exclusive territorial agreement between a brewer and a wholesaler.

It invites expense and endless litigation, and forces the wholesaler to risk his big investment, and his employees their jobs, against devastating "free-riders" who transship from market to market.

Let us briefly and realistically demonstrate why.

Suppose brewer Thomas enters into an exclusive territorial agreement covering a medium size city with wholesaler Wilson. They make the agreement for a term of four years. Wilson has to build a warehouse, purchase trucks to serve the retailers in that city, and employs drivers to deliver that brand of beer. He must also rotate the retail stocks, and take back any stale beer.

Another licensed wholesaler in the same state wants to transship into Wilson's territory, and to cream Wilson's market by selling trailer loads to the largest retailers in Wilson's territory.

To clear the way, he brings a private antitrust lawsuit, charging that under Sylvania the exclusive territorial agreement violates the antitrust laws. To litigate that lawsuit would require prolonged depositions, and a long and costly trial for Wilson to defend his investment and his employees' jobs.

That litigation might well take several years. Even if Wilson ultimately wins, he may be broke. To say that the Sylvania opinion protects him is a sham.

Let us once again concretely demonstrate why that suggestion is fallacious.

Judge Posner in his brilliant study of restricted distribution and the problems of the Sylvania rules pointed out all of the ambiguity and difficulties in that opinion. Posner, "The Next Step In The Antitrust Treatment Of

Restricted Distribution, 48 University of Chicago Law Review 6 (1981).

He termed the "rule of reason" in these distribution cases as utterly vage and an intellectual vacuum. He demonstrated that it imputed to juries and judges powers of analysis that most of them lack to apply to so poorly articulated a standard. In his words, "it places a considerable hazard on any restriction that a manufacturer imposes on its dealers or distributors." (P. 15) Other antitrust writers agreed.

Moreover, any examination of the relevant lawsuits since Sylvania proves that point conclusively. In many of them, treble damage judgments approaching $500,000 were awarded by juries, only to have the cases reversed after arduous and costly appeals.

We invite examination of three of them:

Oreck v. Whirlpool in the Second Circuit Court of Appeals, 579 F.2d 126 (1973), where a massive treble damage judgment was reversed by a divided court.

Borgen v. Yamaha in the same circuit, decided in 1980 (625 F.2d 390), where a jury judgment over $450,000 was again reversed and remanded.

Muenster v. Stewart in the Fifth Circuit in 1981, where distributors of Zenith Radio had been assigned exclusive areas, the jury, after a lengthy trial, awarded $150,000, and the Court of Appeals reversed it (651 F.2d 292) after a costly appeal.

Two other observations are pertinent. Lawsuits since Sylvania certainly offer a lucrative field day for lawyers who bring antitrust treble damage cases for any distributor who doesn't get a franchise.

Second, the Committee will readily appreciate that where malt beverages are concerned, such litigation will also involve the Twenty-First Amendment and all of the uncertainties of the Midcal decision and the complicated constitutional issues on the collision between antitrust law and the Twenty-First Amendment.

S.1215 is therefore necessary. That necessity is acute in the distribution of beer. Absent the narrow protection the Bill will afford to territorial arrangements, the economic evil of transshipping will continue to destroy the beer wholesalers.

It is no answer to suggest that if a small businessman gets a competent antitrust lawyer, he can after years of litigation and massive legal cost eventually succeed on an appeal.

VI. The Objections Of The Department Of Justice Do Not Justify Rejection Of The Malt Beverage Interbrand Competition Act, S.1215

Under date of April 13, 1982, the Assistant Attorney General of the Department of Justice, Office of Legislative Affairs, filed with the Chairman of the Committee on the Judiciary a letter setting forth the Department's asserted reasons for opposing the enactment of S.1215, the "Malt Beverage Interbrand Competition Act."

The Department's letter reflects only theoretical and unfounded economic objections, misstates the provisions of the Bill, is internally inconsistent, and does not respond to the realistic need of malt beverage wholesalers to be protected against future complicated costly private treble damage litigation.

I.

The Department's basic position is that exclusive territorial distributorships "usually serve legitimate purposes" but "might be used for anticompetitive purposes in certain special circumstances." (p. 2.) Throughout the letter, theoretical fears of adverse competitive effects are expressed only as "may" or "might." In contrast, the letter concedes the basic need in the malt beverage industry for product promotion, quality control, and point of sale services to protect the quality of beer offered to consumers. It also acknowledges the "free rider" problem in the distribution of malt beverages. (p. 2.) Finally, it is stated that

> "The Department recognizes that exclusive territorial arrangements have beneficial effects in a wide range of market settings."

and considers

> "such arrangements as legitimate in most cases." (p. 3.)

II.

The Department's objections focus on a "might be argued" concept that a narrow legitimizing of territorial agreements under Federal antitrust law (in the present confused state of that law) might facilitate collusion among wholesalers.

This unfounded and fallacious assumption is readily answered. In the first place, as Section 3 of the Bill makes clear, and as the Department admits, the Bill in no way exonerates any attempted or achieved collusion among wholesalers. As the Department's letter states it,

> "We recognize that the antitrust laws would potentially be available to challenge actual collusion among competitors even if S.1215 were enacted."

Accordingly, the Department's objection is not related to S.1215, and instead seems to be based on the asserton that where there is unlawful collusion, not exonerated by the Bill, the Government would have difficulty or be inept in proceeding against it.

There is no suggestion that any private litigant would encounter the same difficulties. Put another way, the Department admits that S.1215 is not in any sense an exemption from basic antitrust law, but is instead a narrow and needed protection for beer wholesalers in the many situations where "free riders" are increasingly destroying their capacity to continue in business and to maintain their investments and employment.

III.

The letter relies upon the pending case of Norman Williams in the United States Supreme Court. It suggests that the aberration in the involved California statute will readily be corrected. Even if the Supreme Court agrees, that possibility only confirms that Section 3 of S.1215 fully sustains the applicability of all basic antitrust prohibitions to the distribution of malt beverages. Obviously, if collusion among wholesalers exists, there is not the "substantial and effective" interbrand competition required by Section 3 for the Bill to be operative.

IV.

The Department's letter also attempts to distinguish the comparable Soft Drink Interbrand Competition Act on the ground that the Department had objected to that statute. The letter refers to deregulation of highly regulated industries, such as airline, trucking, and railroads; but it completely disregards the effect of comprehensive state regulation of the distribution of alcoholic beverages, including beer, within each state under the Twenty-First Amendment. Further, the Department's letter in no way acknowledges that the Midcal case (445 U.S. 97 (1980)) confirms that Section 3 of S.1215 fully covers any violation of the antitrust laws which it specifies.

Thus Section 3 preserves the full right of the Government and any private litigant to challenge under the Federal antitrust laws any collusion among either brewers or the wholesalers for whose protection the Bill is proposed.

V.

In short, the Department wishes to retain its opportunity and that of private litigants to mount costly litigation

> "where their [exclusive territorial arrangements] procompetitive utility outweighs such anticompetitive risks as they might contain." (p. 7.)

It expresses "its willingness to explain the utility of vertical territorial arrangements to courts . . . in private treble damage actions." Instead of statutory protection for legitimate and essential business arrangements, it wants the option of intruding into private lawsuits, in which obviously the Government is not a party, whenever and wherever it wants to do so.

The Department thus attempts wholly to sidestep the demonstrated underlying need for S.1215.

Beer distributors may not rest easy because the Supreme Court has recognized that vertical territorial restrictions have obvious pro-competitive effects in markets such as theirs. Nor are they protected by the various State laws that expressly make permissible or mandatory such arrangements in the beer industry.

Instead, the lure of treble damages and the potential for "Rule of Reason" litigation can and recently has resulted in numerous private antitrust challenges. Malt beverage distributors may thus be subjected to serious financial burdens in private damage suits regardless of whether they can eventually be shown to promote competition under existing law.

Realistically, where a beer wholesaler under an exclusive territorial arrangement operates for a number of years, under existing law he can be made to defend his previous conduct in a treble damage action by another wholesaler who was not given an exclusive territorial arrangement, or by a "free rider" located elsewhere who wants to invade his market. The suggestion that if his past conduct is judged by the Department of Justice to have been proper under the Rule of Reason, the Department might intervene in the private lawsuit to help him is as theoretical as the apprehensions of the Department. No businessman with a massive investment who provides large employment within his distribution territory should be subjected to those risks. If his conduct goes beyond what S.1215 permits, the full panoply of antitrust remedies, including both Government prosecution or private challenge, remains available.

VII. The Objection Of The Federal Trade Commission To S.1215 Is Unfounded

The Federal Trade Commission's objections to this Bill, in its letter of June 11, 1982 to the Committee, are difficult to comprehend and insubstantial.

In the first place, the Commission concludes that any substantial analyses by it of "either of the nature of exclusive territorial arrangements or of competitive conditions in the malt beverage industry" are unnecessary. In no way does the Commission address the problems of transshipment which have been abundantly demonstrated to destroy the distributors of malt beverages.

The rhetorical conclusion is that the Commission opposes the Bill because "sometimes" exclusive territorial arrangements may be anticompetitive.

Nor does the Commission in any way approach the problem of the conflict between the Twenty-First Amendment, where state law permits or mandates exclusive territories for wholesalers of alcoholic beverages, and the *Midcal* decision which created the present uncertainties about the application of that decision to these distributors.

Finally, attached to the Commission's letter is a supposed economic analysis of beer distribution.

This largely supports the Bill. The Commission suggests as a generality that to solve the "free rider" problem, the brewer may perform distributing services itself or even assign exclusive territories. This is an economic fantasy in view of the licensing system for alcoholic beverages in each state.

The Commission fears collusive arrangements among wholesalers but completely fails to recognize interbrand competition. The short answer is Section 3 of the Bill, which is no way immunizes horizontal agreements by anyone.

Finally, the FTC recognizes that competitive conditions in some industries makes it

> "relatively difficult for firms to use exclusive territorial arrangements in anticompetitive ways."

Yet the Commission concludes by saying that

> "We do not have reliable data on the structure of the malt beverage wholesale distribution sector." (P. 8)

In short, the Commission's objections are merely speculative. Thus, wherever the FTC may believe that there is not substantial interbrand competition in any industry, it still wants to be free to charge that exclusive territories, standing alone, are illegal.

Confronted with their present problems, beer distributors must be left free from that type of administrative harassment.

Mr. **Podolsky**. S. 1215, the Malt Beverage Interbrand Competition Act, is a simple clarification of the 21st amendment to the Constitution of the United States. Parenthetically, it is amazing to me that neither Professor Kahn nor Mr. Lipsky have devoted much time or attention to the 21st amendment except to say we have been living under it for some 50 years. And I am not sure whether it was 50 schizophrenic years or what. But I am not sure what the prediction will be for the next 50 years, either.

Nonetheless, the 21st amendment simply states that exclusive territorial agreements—no. The Malt Beverage Interbrand Competition Act simply states—and this is important—that exclusive territorial agreements between wholesales and brewers do not violate Federal antitrust laws so long as there is substantial competition from other brands in the defined territory. And that is the gist of this bill.

The 21st amendment is totally unique in the constitutional scheme in that it represents the only express grant of power to States. In all other areas of State legislation or regulations, State power is limited by the Supremacy Clause in the Federal Constitution. State law regulating intoxicating liquors is in a different status. Statutes falling within the framework of the terminology of the amendment achieve constitutional status, are entitled to the presumption of validity, and have been and should continue to be upheld by the courts, whether State or Federal.

There is no doubt about the intent of those who framed the amendment. As originally proposed, the resolution contained three substantive sections, the third of which provided, and I quote: "Congress shall have concurrent power to regulate or prohibit the sale of intoxicating liquors to be drunk on the premises where sold."

That section was deleted because of the realization that it could be used to deprive the States of the power granted to them by the second section. As one Senator pointed out, "We would expel the system of national control through the front door, section 2, but readmit it forthwith by the back door of section 3."

The amendment, therefore, was passed with only two sections. The first repealed the 18th amendment, which had established National Prohibition; and the second, the important section, specifies: "The transportation of importation into any State, territory or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited."

Clearly then, the regulation of intoxicating liquor business within a State boundary is delegated to the powers of the State by the 21st amendment.

Senator **Laxalt**. That is not the exclusion of the Feds under the Sherman Antitrust Act?

Mr. **Podolsky**. That came a little later, Senator, that is true. It is true that this was enacted 50 years ago.

Senator **Laxalt**. So, whatever is done on a State level, it is still subject to the overall umbrella of the act?

Mr. **Podolsky**. Absolutely.

In one of the first leading decisions under the 21st amendment, *Board of Equalization* v. *Young's Market,* the Supreme Court held that the constitutional provision gave to the States the right to determine the extent to which and the conditions under which intoxicating beverages may be brought into the State for the purpose of sale and that it freed the States from all restrictions upon the police power to be found in other provisions of the Constitution.

There are always conflicts between provisions of the Constitution. The 21st amendment clearly delegates to the States the right to regulate and control the liquor business with the State. Then there will be a conflict between that and the police power or that and the commerce clause, antitrust law.

The *Young's Market* case has been construed as meaning that a State is totally unconfined by traditional commerce clause limitations when it restricts the importation of intoxicants destined for use, distribution, or consumption within its borders.

The States wide powers under the 21st amendment and other provisions were recently reaffirmed by the Supreme Court in *California Retail Liquor Dealers Association* v. *Midcal Aluminum, Inc.* Again, the court recognized that Congress power under the commerce clause is qualified—Mr. Lipsky would say they would weigh the balances—by section 2 of the 21st amendment and specifically held: "The 21st amendment grants States virtually complete control over whether to permit importation or sale of liquor and how to structure the liquor distribution system."

The major significance of the *Midcal* decision is that it provides two guidelines for price regulations. State legislation enacted in reliance on the 21st amendment must include requirements for active participation of the State alcoholic beverage agency and must serve a legitimate State purpose such as traditional police power objectives or preservation of State revenue.

This and comparable holdings have been repeated throughout the years, but they have not always been applied to the full extent that the words of the 21st amendment might justify. Some erosion of the concept of State power has resulted from courts placing particular emphasis on the exact terminology the amendment itself.

Even for products not afforded the specific protection of the 21st amendment, nonalcoholic products, the legal principles applicable to territorial agreements and other vertical arrangements between a manufacturer and his distributors not involving prices were established by the Supreme Court in *Continental TV* v. *GTE* Sylvania. The court there reconsidered its earlier decision in *United States* v. *Schwinn* and held that vertical nonprice arrangements entered into by wholesalers and manufacturers do not per se violate the Sherman Act but, instead, must be evaluated in each case through the rule of reason, which you have heard about, based upon a detailed factual assessment of the reasons for and the economic consequences of the arrangement. In so holding, the court recognized that the goals of competition are most effectively fostered by promoting vigorous interbrand competition. The court made a specific statement to that effect, that competition is most effectively fostered by vigorous interbrand competition.

In turn, the court acknowledge that interbrand competition is often best promoted by permitting manufacturers and wholesalers to enter into vertical nonprice arrangements.

Mr. Lipsky referred to Judge Posner's article in the University of Chicago Law Review. Well, we take a somewhat different view of that article than he presented. Judge Posner, in his brilliant study of restricted distribution and the problems of the Sylvania rules, pointed out all of the ambiguity and difficulties in that opinion. In his article in the University of Chicago Law Review, Judge Posner termed the rule of reason in these distribution cases as utterly vague and an intellectual vacuum. He demonstrated that it imputed to juries and judges powers of analysis that most of them lack to apply to so poorly articulated a standard. In his words: "It places a considerable hazard on any restriction that a manufacturer imposes on his dealers or distributors." And other antitrust writers have agreed.

Since Mr. Lipsky quoted Judge Posner, we felt it important to bring that to your attention.

Back to the *Sylvania* case. The court identified several important redeeming virtues of such vertical nonprice restrictions. For example, new manufacturers or manufacturers entering new marketing areas may have to give wholesalers exclusive territorial areas in order to encourage the wholesalers to risk the large and essential investments of capital and the employment of labor. Similarly, established manufacturers often need such arrangements in order to encourage their wholesalers to engage in adequate promotional activities, to provide proper servicing of retailers, and to insure appropriate quality control in the interest of consumers. This is all part of the opinion.

The court also recognized that, unless appropriate servicing and quality control by wholesalers can be insured, a manufacturer's goodwill and the competitiveness of his products may be adversely affected. It acknowledged that, because of the problem of free riders and other market imperfections, such services may not be provided by wholesalers unless they are given suitable territorial protection. Further, the court noted that manufacturers have, in any event, an economic interest in maintaining as much intrabrand competition as is consistent with the efficient distribution of their products. In other words, the manufacturer will not allow noncompetitive intrabrand situations to exist.

Based upon these and other considerations, the court held that vertical nonprice restrictions are not per se violative of the Sherman Act. To the contrary, the court emphasized that such arrangements are widely used in our economy and that their economic utility is confirmed by extensive scholarly writings and numerous judicial decisions. The court concluded that the lawfulness of such arrangements should be determined on a case-by-case basis under the rule of reason.

So, with the 21st amendment and with the *Sylvania* case, why then are we asking for this legislation?

The existence of those principles established in the 21st amendment, *Midcal* and *Sylvania* do not diminish the need for adoption of the proposed Malt Beverage Interbrand Competition Act. The reason is that antitrust litigation conducted under rule of reason principles is inevitably lengthy, burdensome, and expensive.

Senator LAXALT. How much litigation has there been along these lines?

Mr. PODOLSKY. On page 10 of the document we submitted we have listed 25 cases. The Federal courts frequently have applied and interpreted *Continental TV* v. *GTE-Sylvania, Inc.* The following list includes examples of such cases decided by each level of the Federal courts. The approaches taken by these courts often have not been consistent. There are 25 cases here. Plaintiffs prevailed and received a money award in the following vertical or partially vertical cases. There are three more cases here. The cited opinions are the most recent opinions found in each case and usually are not the opinions in which a liability was initially found.

In other words, it is easy to find initial liability for the judge and jury. These are appellate cases. So, we have a list of 25. It is in our document on pages 10, 11, and 12.

Such litigation is extremely expensive. It requires a detailed examination of the specific conditions and circumstances of each of the particular local markets involved. Elaborate discovery and the presentation of expert economic testimony are virtually unavoidable. Even where, as in cases involving the distribution of malt beverages, the ultimate reasonableness of the vertical agreements appears clear from the outset, a court cannot realistically be expected to resolve the issue without long proceedings and often a lengthy trial.

The proposed act would serve the public interest by confirming the lawfulness of territorial agreements, by adding to the law an important and necessary degree of certainty, and by avoiding the costs and burdens of needless litigation. Such costs and disruptions must inevitably fall upon consumers in the form of increased prices. Without significantly altering the law or the results of such litigation, the proposed act would clarify and confirm the principles established in *Sylvania*. We will not significantly alter the law whatsoever.

Recent litigation emphasizes the need for this clarification. Mr. Lipsky referred to *Rice* v. *Norman Williams Co.* The decision is pending, as he told you. Another case is *Colby Distributing Co.* These principles of the rule of reason were thoroughly confused. The *Rice* case is a California case. The *Colby* case is a Kansas case. In both of these cases, State statutes were attacked as violations of the Federal antitrust laws. Applying similar reasoning, the courts of California and Kansas reached totally opposite conclusions. Therefore, we believe Congress should speak on this matter and clear up this confusion.

In the *Rice* v. *Norman Williams* case, the Justice Department came in as amicus curiae because the court in California had substantially misinterpreted the prevailing law and had substituted a per se test instead of a rule of reason test. Even the Government intervened in that case.

So, there is a great deal of confusion. But we cannot always depend upon the Justice Department to intervene in every case that we feel is necessary.

It is extremely important to note that the enactment of S. 1215 will serve to protect all existing State statutes on territories. It will not disturb existing State laws. Most States recognize the rights granted by the 21st amendment and the *Sylvania* case. Twenty-five States have passed statutes requiring or implying exclusive sales territories for beer wholesalers; another 12 States have statutes permitting such territories. The remaining States have not yet passed legislation in this area, but legislation is pending in several of them. We have an appendix of this attached to our record. Only the State of Indiana has a regulation prohibiting exclusive territories.

Passage of this legislation will not affect any of these State statutes; regardless of what Professor Kahn said, it will not affect any State statute, nor will it require any changes in any State statutes, nor will it require any States that do not have a law to enact a law. The States have complete prerogative to enact whatever law they feel better. The question of whether an exclusive territory law should be enacted or not will be fought out in the State legislature instead of being fought out in other areas.

We firmly believe that the consumer's best interest relative to malt beverages is being served by his State legislature. This bill will preserve that local right of self-determination, be it that which was recently reaffirmed by the regulations of Indiana or my own State of Michigan. In Michigan, public policy requires not only exclusive territory for beer wholesalers but also requires us to initiate the mandatory container deposits, to engage in recycling and to act as an agent for the State in collecting excise taxes. We believe that the 21st amendment clearly intended that the several States should be able to impose these or any other requirements they deem proper in their own public interest.

Therefore, the purpose of the proposed Malt Beverage Interbrand Competition Act is to clarify and confirm existing principles of constitutional law and an important area of public policy. While the principles declared in *Sylvania* should insure the lawfulness of exclusive territorial agreements for the wholesaling of malt beverages, those principles still permit lengthy and expensive litigation. As the lower court decision in *Norman Williams* illustrates, those principles may be misunderstood and misapplied.

Confirmation of *Sylvania* by the proposed act, like Congress confirmation of it last year in connection with soft drink wholesaling, will serve the public interest in several important respects. Needless and costly litigation will be avoided, uncertainty and confusion will be dissipated, and the regulatory authority of the States will be reemphasized. Vigorous interbrand competition will be maintained and strengthened. Significant local businesses, offering employment and other benefits in areas throughout the country, will be given reasonable protection. Consumers will continue to be assured prompt and economical distribution of malt beverages of high quality.

Failure to pass S. 1215 will continue to put all of the current State laws in legal jeopardy in contravention of the 21st amendment. Public policy related to alcoholic beverages as a part of the general free market system is clearly set forth in the supporting statement of the U.S. Treasury Department in regard to the draft amendments to the FAA Act. I quote:

"Prior to prohibition alcoholic beverages were treated like any other product of commerce at the Federal level and was afforded protection from State imposed restraints under the Commerce Clause."

"In repealing prohibition, however"—the 21st amendment—"the Congress recognized that to return to the preprohibition policies was unacceptable. Two important steps were taken. First, the States were given constitutional protection for their local regulation of alcohol; and, second, the Federal Government stepped in to regulate the competitive pressures which led to a disregard of State policies in the past."

Clearly, gentlemen, malt beverages were never intended to be treated like corn flakes or similar products in general commerce. They are highly regulated, they are highly controlled substances. Every step of the process from brewing to retailing, indeed the very definition, the legal definition of what constitutes beer, is subject to intense regulation and control. There are a multitude of licensing and regulatory requirements in every State, all different. The States right to exercise these controls must be protected and reaffirmed by passage of this legislation.

In response to what Senator Metzenbaum said and to what Professor Kahn said, this law is not an exemption from the antitrust laws. It is not an exemption whatsoever. In the first place, it merely gives the States the power to enact exclusive territory laws. It does not mandate it whatsoever. Second, it codifies the prevailing consitutional law regarding the 21st amendment and the *Sylvania* case. It protects against needless and expensive litigation. Most important of all, all the antitrust remedies that were available before the enactment of this law are still available except that the existence of an exclusive territory agreement between a wholesaler and a brewer is not per se an indication of a violation of the Sherman Act. That was already enunciated by the court in the *Sylvania* case.

So, this is not an exemption in any fact or manner at all.

Professor Kahn, with all due respect to his academic brilliance and analysis, was off base and did not have to pay the thousands of dollars that we small businessmen have to spend to prove we are not violating the rule of reason. What I am trying to say is, when he says the rule of reason where it is right, that is an invitation for a good antitrust lawyer or a bad one, or an antitrust lawyer 'to initiate a suit against a wholesale. And a wholesaler has to defend it. It is a very expensive process. That is what we are trying to get out of.

Gentlemen, I would like to ask my colleagues to testify. Mr. Lara?

Mr. LARA. Thank you. Mr. Chairman, my name is Edison R. Lara, Sr. I am the president of Westside Distributors, located in Los Angeles, Calif. We have been in business for 8 years. It was an existing business. We started out with 12 employees, and today we employ over 60 people full time. I would like to comment briefly on the manner that wholesale beer distributors operate in the State of California.

In California there is a law that is supported by rule 105 of the Alcoholic Beverage Control Act. That act has two primary parts. Rule 105 permits the manufacturer or importer to assign primary areas of responsibility. The rule also requires each wholesale beer distributor to post with the Department of Alcoholic Beverage Control the prices that the company will sell to the retailers that it services. The price postings are made by county.

The posted prices are for sales starting with case one and does not allow for quantity discounts. This method allows the smaller retailer to purchase at the same price as the largest retailer, thereby keeping the smaller retailer competitive with the major or larger retailers.

The retailers are, of course, free to set their prices to the consumer. The present rule has been in effect since 1951 and is in major part responsible for a very orderly market. There is, to be sure, very intense interbrand competition among the wholesalers throughout the State.

A survey was recently conducted by the California Beer Wholesalers Association regarding consumer prices for beer throughout the United States. The results were very gratifying in that the prices paid by California retailers and consumers are among the lowest in the Nation. In my opinion, this speaks well for the present system. The retailers and consumer are receiving excellent price to value purchases.

The three-tier system is being conducted in a very competitive and orderly marketing environment. I also might add that there is a volunteer recycling program in effect throughout the State with most of the wholesale beer distributors.

Thank you for allowing me to make these observations on the method of doing business in the State of California.

Senator LAXALT. Thank you very much, Mr. Lara. Mr. Nunnelee?

Mr. NUNNELEE. Thank you, Mr. Chairman. My name is Lewis Nunnelee. I am from Wilmington, N.C. I operate Coastal Beverage Co. there. We are a Miller distributor. I have been in the beer business since 1953. I started my own business in 1960. We started with 2½ routes, and now we are up to 16 routes.

Fortunately, I have two sons in the business with me. One son is here today. He is our general manager. He is 31 years old. Hopefully, in a few years, when I get so mean and cantankerous that they want to get rid of me, then he will take it over and carry it on for me.

We are family owned. My wife and I own 75 percent of our business; my children own 25 percent.

The State of North Carolina grants us territorial rights now. We have still got a lot of dry areas in the State of North Carolina, like they do in many of the Southern States. I cover some seven counties. Out of those seven counties, three are wet; and the other four counties are dry counties. Some of them have some wet townships in them. So, the territory that I cover has a lot of dry area in it. We have got a lot of mom and pop stores out in the country, general stores, service stations, this type of thing. In fact, the big chain supermarkets only represent 24 out of 1,153 accounts that we service. We are in a rural area, I guess you could say.

Since North Carolina is in the Bible Belt, we need strong regulation. If we had not had it through the years, our whole State would have been dry. I came in the business in 1953, and most of the State was dry. We have worked very closely with our State board of alcoholic control to make sure that we had stringent regulations, and we abided by these regulations. So, we have good law in the State of North Carolina. It has been our salvation, I think, to keep the State available for being a distributor.

I might say that the State of North Carolina has an excise tax of $1.20 per case. That is 5 cents for every 12-ounce can or bottle of beer. It is a pretty heavy tax. I think South Carolina is the only State in the Union that is higher taxed than we are. We, as distributors, collect this tax for the State of North Carolina.

From a competitive standpoint, we are fiercely competitive and always have been since I have been in the business. We have got exclusive territories. In my territory, I overrun several Budweiser distributors, several Schlitz distributors, Pabst. So, we do overrun each other in our exclusive territories.

We are fiercely competitive. Every morning when we walk out the door, we fight like mad out there. So, I do not think that that is a good argument.

As Miller distributors, we are expected to abide by certain brewery expectations. We are expected to keep a good image in the community. We have a controlled temperature warehouse. Our warehouse is 38,000 square feet. They want that product to be at its peak when it reaches the consumer. We keep our product in these controlled temperature circumstances. That is one of their requirements.

We are required to keep updated equipment to keep our image before the public. Once a year we file a 5-year plan with our brewery showing what we are going to be doing the next 5 years in the way of personnel, equipment, warehousing, financing, so that they know this product is going to be available to the consumer. This assures the consumer of getting a quality product down the road.

I have heard it alluded to about the fresh beer aspect. Our requirement with fresh beer as a distributor, our brewery puts a marking on each can and bottle that shows you just like a loaf of bread or a bottle of milk when the pull date is, when that beer goes out of date. We have to have it off the retailer's shelf by that date. We have a brewery rep that polices this. We have to dump this product if it is over 120 days old.

I guess my point, Mr. Chairman, is that we are highly competitive. We are operating now under an exclusive territorial arrangement. If it had not been for that, we would probably have been dry. Thank you.

Senator LAXALT. I think your testimony is terribly significant because you are apparently under very difficult circumstances—Bible Belt and many other problems in that part of the South. Nonetheless, you have obviously put together and maintained a very successful business. You are competitive. You have a territorial arrangement which apparently is working satisfactorily. The situation would not result in any particular loss to the consumers.

Tell me, why do you need Federal legislation? You seem to be getting along very well.

Mr. NUNNELEE. We do not need it in North Carolina, Mr. Laxalt I guess the only time we would need it if somebody came in and threw a lawsuit at us. Then we would have to go into costly litigation.

Senator LAXALT. The point was made before that there is a vulnerability to which you now are exposed. That kind of litigation would be very protracted and very expensive. You want to remove that area of vulnerability. Is that it?

Mr. NUNNELEE. Yes.

Senator LAXALT. Are there any other compelling reasons why people on your level would need this legislation?

Mr. NUNNELEE. None that I can think of, not where I sit in North Carolina. We have got a good system going for us right now.

Senator LAXALT. The committee has been told—and I would like some remarks from any of you on this—that the experience of the soft drink industry has been a rather drastic increase in consumer prices. They contend that we would have the same result here. May I have some opinions with respect to that?

Mr. RUSSELL. Mr. Chairman, you only have that trouble where you had increase in pay due to union programs. That is the only reason.

Mr. PODOLSKY. Basically, a beer wholesaler only works on a 20- to 22-percent margin on the sales price. Eighty percent of his cost is determined by the brewery. He buys his beer from the brewery. We cannot sell any cheaper than we buy it for. I know in our business, and I think it is a general average for wholesalers, they average around 2 to 2.5 percent of the gross sales in profit, net profit. That is an average figure. So, out of the 22 percent that we have in our control, so to speak, our margin of profit, we average 2 percent on our own; 20 percent goes out in expenses, labor expenses, warehouse expenses, sales promotion expenses, taxes, excise taxes. And that is all part of our operating problem.

The reason we have to spend that much in sales expense and promotion expense is that we have a very delicate relation with our brewery. We want to do as much as we can to promote the sale of our brand of beer. The brewery wants to make sure that we do as much as we can to promote the sale of that brand of beer. So, I am out there fighting against that other guy every chance I can. I have to promote that beer. I have to protect the quality of the beer, as Mr. Lara does and everybody else does. I am not unique; everybody does it. We all have the same expenses in a given area.

In my area we all have the same union. We all have substantially the same warehouse except that his has to be larger. In order to be a Miller, Budweiser, or Stroh distributor now, you have to have a warehouse that can carry 45 days' inventory and it has to be temperature controlled so that you can store beer in the wintertime for the breweries which they can produce at cheaper—by being able to give a 45-day supply, a brewery can accumulate beer in the distributor's warehouse which will enable them to even out their production year round. Instead of producing a lot of beer in June and July, they produce it at a more even rate, which is a much cheaper method of production for the brewery and insures cheaper prices to the consumer.

All of these expenses are part of our business. I have just been informed that later Mr. Sellinger will address this in more detail, so I will not take up your time.

Senator LAXALT. I guess the essence of your position is that this would not result in increased consumer costs?

Mr. PODOLSKY. No, sir, the Interbrand Competition Act will result in lower consumer costs because we will be able to operate more efficiently. The brewers will be able to operate more efficiently. The public will be served by a better operation.

Mr. LARA. We will be able to maintain good quality control, Senator.

Senator LAXALT. Thank you. I appreciate your help.

We will now have another panel consisting of Mr. Frederick Meijer, vice chairman of the Food Marketing Institute here in Washington; Matthew Protos, president of the National Licensed Beverage Association from Alexandria, Va.; and Mr. Mac Greer, president of the Alabama Retail Association, Montgomery, Ala.

I might say, Mr. Greer, that Senator Heflin left with me a statement which I will introduce in the record so you will not feel you are here all by yourself. It is as follows [reads].

> Mr. Chairman, it is a great pleasure for me today to introduce a fellow Alabamian, Mr. Mac Greer, to this committee. Mr. Greer is vice president of Autry Greer & Sons, a food retailer and wholesaler based in Mobile, Ala. His company was founded by Mr. Greer's grandfather in 1916 and has grown to where it today operates 34 grocery stores in Alabama and serves hundreds of independent grocers in Alabama and Mississippi. In addition to his work with Autry Greer & Sons, Mr. Greer is currently serving as president of the Alabama Retail Association. It is largely in this capacity that he is to testify before this committee today to present the opinions of the thousands of food retailers across the State of Alabama.
>
> I am confident Mr. Greer's experience and expertise in the area of food retailing has enabled him to assemble a fine statement. I am certain it will be a great deal of help to this committee in its deliberations on Senate bill 1215. Thank you, Mr. Chairman.

STATEMENTS OF A PANEL CONSISTING OF FREDERICK MEIJER, VICE CHAIRMAN, FOOD MARKETING INSTITUTE; MATTHEW PROTOS, PRESIDENT, NATIONAL LICENSED BEVERAGE ASSOCIATION; AND MAC GREER, PRESIDENT, ALABAMA RETAIL ASSOCIATION

Mr. MEIJER. Mr. Chairman, I am Fred Meijer. Thank you for inviting us here.

Senator LAXALT. We are delighted to have you here, Fred.

Mr. MEIJER. I am vice chairman of Food Marketing Institute, but I do not make my living there. I make my living as chairman of Meijer, Inc., and we have 34 supermarkets in the State of Michigan.

It is interesting that I may be following one of our suppliers from the State of Michigan; I am not sure. I would have looked it up had I known he was going to precede me.

I started in this business 48 years ago when I was 14 years old. One of my first jobs as soon as Michigan beer was legal was handling beer bottles. So, I have handled them for a long time.

FMI appreciates the opportunity to testify in opposition to this bill, S. 1215, the Malt Beverage Interbrand Competition Act, or, more accurately, the Beer Monopoly Protection Act, as we see it. As a retailer, I also appreciate being invited to testify here.

FMI is a nonprofit trade association whose over 1,100 members are food retailers and wholesalers of all sizes. The membership includes independent grocers, food chains, and also voluntary and cooperative wholesalers. More than half of FMI retailer members are single-store operators.

We have prepared an extensive document complete with legal analysis and citations which, I believe, is extremely persuasive in demonstrating why S. 1215 is simply a bad bill. The document is also long. In the interest of saving your valuable time, I would like to summarize the main points of the document.

The Malt Beverage Interbrand Competition Act is not about competition. It is about the fear of competition. Under the guise of clarifying the antitrust laws, this bill will protect the profits of the beer industry to the detriment of the consumers. It is anticompetitive and anticonsumer. And we the retailers have the operational problems and our customers pay more for their beer. While the distributors, as one man said at the table here, have an orderly market, the retailers do not; and the consumers pay more.

Senator LAXALT. This is as fundamental in importance as it can be. They contend that passage of this act would not in any way mitigate the interbrand competition within the respective States. I gather you disagree with that.

Mr. MEIJER. Completely. And I hope to point that out later.

Senator LAXALT. Please do that because it is terribly important for the consideration of this committee that that point be developed.

Mr. MEIJER. If I do not make it clear, I hope you ask me the question so that I do make it clear. Please do.

This bill is not only unnecessary but affirmatively harmful for several reasons which we will address in turn. The bill would decrease service and increase costs to the retailers. Exclusive territories in the beer industry have been found to increase prices to consumers by as much as 20 percent. And make no mistake about it; the intent of and the end result of this legislation is to promote exclusive territories in beer distribution.

Senator LAXALT. Where is the data to support that contention? The committee has been informed many times that this could result in a 20-percent increase to the consumer. Do you have something authoritative to support that?

Mr. MEIJER. I believe we have some information.

Mr. GREER. There is going to be a panel of Indiana people later on.

Senator LAXALT. They will speak to us based upon their experience?

Mr. GREER. Yes, Mr. Chairman.

Senator LAXALT. Very well.

Mr. MEIJER. By the way, Mr. Chairman, we do have exclusive territories in Michigan now under which we are operating; so that is the framework where I personally operate. We understand the problems that this has caused.

Senator LAXALT. Do you have data developed in Michigan indicating the exclusive territory arrangement within Michigan that has resulted in these increases in consumer prices?

Mr. MEIJER. Yes, we do. I could skip to it now.

Senator LAXALT. No, that is all right. Proceed in any fashion you want.

Mr. MEIJER. The beer industry has not been the subject of any court decisions, as the soft drink industry was, in which exclusive territories were found to be illegal under the conditions of that industry.

No special circumstances render the additional protections of S. 1215 necessary.

The bill would insulate in the beer industry alone conduct that would otherwise be unlawful.

The bill would interfere with State control of trade in malt beverages.

The precedent of this legislation will create considerable pressure for Congress to carve out additional exemptions from the antitrust laws for other suppliers of food and grocery products.

In short, FMI opposes this legislation because it is anticompetitive, inflationary, and, we feel, unnecessary. We believe it would be especially inappropriate for the Congress to enact this protective, special interest legislation now when the virtue of free enterprise is being stressed in other sectors of the economy.

If enacted, this legislation would allow a brewer of a particular brand of beer to enter without fear of antitrust laws into an agreement with a wholesaler giving that wholesaler the exclusive right to sell that brand in the territory.

In Indiana, a State legislative study commission recently determined that the retail price of beer went down 20 percent when that State's law was changed to prohibit exclusive territories and to allow competition among beer distributors. Since almost $10 billion was spent for beer in the food and grocery stores alone in 1980, it is obvious that our consumers have a lot to lose if this bill becomes law.

Exclusive territories diminish the incentive for wholesalers to provide good service and competitive prices to the retailer. The situation is analogous to you as a grocery store customer to be able to shop at only one store in your designated area. Imagine if your grocer were the exclusive distributor of food and grocery products in your neighborhood. Imagine further that a grocer outside your neighborhood is not allowed to sell to you even if you arrive at his store with cash in hand.

What could you do if you are unhappy with the local store's hours? What if the quality of the meat or produce is not acceptable? What if the store's prices are outrageously high? The short answer is that you could do nothing. Now imagine that there is a competing grocer across the street, and there usually is in reality. In which situation do you think the local grocer will be more responsive to your needs and more competitive in his prices?

Wholesalers and brewers argue that because malt beverages have a relatively short life, exclusive territories are needed to insure customer service and protect product quality. This argument is pure nonsense. The shelf life of most beer falls within a range of 75 to 120 days. This is not short life compared to the other products in the grocery stores. Food operators, as a matter of good and standard business practice, institute inventory control and stock rotation procedures to insure good food sanitation and quality. The industry is proud of its record in that area.

We simply do not accept the argument that it takes exclusive territories to insure fresh products. If it does, then milk, eggs, produce and cookie distributors, among others, should be included in this legislation.

Exclusive territories have the opposite effect by limiting the wholesaler's incentive to provide a quality service. Why should a wholesaler be concerned about freshness of product or out of stocks when he has a captive customer? This service problem is especially acute for the smaller retailer who is at the mercy of one supplier. If one monopoly distributor is interested in serving his larger customers, there is absolutely nothing the smaller retailer can do to obtain the product.

I have a list of our problems here. I am going to skip over that and just touch on some of the highlights in the interest of time.

Refrigerated beer was mentioned previously. In Michigan, none of our beer arrives at our stores refrigerated except the kegs of beer in the pony barrels. We have to deal with 18 distributors for our 34 stores, each with either different prices or potentially different prices. Miller High Life costs us in a range from $7.30 a case to $8 a case, a 70-cents spread between distributors that serve our stores. And Old Milwaukee beer also has a 70-cent spread.

In the Detroit metro area, including Ypsilanti, we have five stores. We deal with five different distributors who have at least four sets of prices.

We have a price law in Michigan, which says we may not sell below cost. So, if a distributor across the street is in a different territory and has a lower cost, he can sell to his customers on a special or every day at a lower cost than we are legally allowed to sell to our customers because we pay a higher price across the street to a different distributor.

Then we also have a bottle law in Michigan. We have a mandatory bottle return. In our particular stores we take in 140 to 150 percent more beer bottles than we sell. Therefore, for every hundred cases of beer that we sell, we take in 140 to 150 cases of bottles. We do not have shells to put these bottles in. Many of the places, like gas stations or whoever sells this beer throw away those shells. We understand that is a problem for the distributors. But we have no place to put those bottles. As a result we have to threaten this monopolistic distributor, constantly saying bring us shells or we will stop buying your beer. And, if we stop buying the beer, we will not have the brand.

If the distributor did not have a monopoly on the territory, we are confident there would be a distributor that would be glad to keep us in shells so we had the place to put our bottles.

When this distributor has a strike, we have no place to go and no place to get rid of our bottles. So, we are forced by the State of Michigan to take in the bottles even though we are buried in them at the time. We cannot get rid of them because we must deal with only the one distributor. Whatever the problems the distributor has in his labor relations, we as a retailer are subjected to that.

Competition, we feel, does more to promote quality products and good service than anything else. Retailers who operate in those States with exclusive territories, and we are one of them, as well as open States know for a fact that, where monopolies exist, deliveries are more often irregular or incorrect. Product quality is certainly no better where exclusive territories now exist.

In other words, where there are alternative suppliers, it is important for one wholesaler to treat the retailer in the same way the retailer treats his customers. We both know that if we do not compete we lose a customer. In this situation, we have no place else to go.

This legislation seems to be me-too proposition. The argument boils down: if the soft drink industry receives an exemption from the antitrust laws, why can't we also. There are, however, important differences between the two industries, the soft drink and the beer industry, which are detailed in our full statement. In sum, in the beer industry distributors do not have large capital investments. Product quality is not a major problem. Advertising promotion is not dependent upon the distributor's expenses. Manufacturers, the brewers, do spend extraordinarily large amounts to create the demand for their product. As a result, exclusive territories simply provide a free ride to the designated monopolists.

Because there is no uniform nationwide distribution system for beer no decision could threaten the kind of disruption that was facing the soft drink industry. In fact, there is no pending case at the FTC or at the Federal or State courts or anywhere that would mean the end of all exclusive territories in the malt beverage industry. We certainly wish there could be a change in Michigan. But with the Federal law we will never get a change in Michigan.

Thus, enactment of this legislation is not necessary to protect beer distributors. It will only upset the status quo in beer distribution.

The retailer now cannot buy directly from the distributor anywhere. The existence of the three-tier system of distribution for malt beverages already gives beer distributors a degree of competitive protection that is unique. This means that the State laws or regulations require the maintenance of three totally independent levels of distribution. The brewer may not directly sell to us, the retailer. Rather, the brewer must sell to an independent wholesaler, who in turn sells to a nonaffiliated retailer. In other words, the wholesaler now is guaranteed a spot in the distribution system free of much of the competition that wholesalers of other products face.

The three-tier system already protects the wholesaler from new competitive approaches to distribution, approaches that may very well be more efficient than the existing means of distribution. Exclusive territories go beyond that and protect the wholesalers from competition from other wholesalers.

This bill could immunize anticompetitive activity. Attached to this statement is a legal analysis of this bill which explains the law of exclusive territories generally and as it applies to the beer industry specifically. While I am not an attorney, our lawyers argue persuasively that the law in this area is clear and that it causes no special problems for beer distributors.

With this legislation, the beer industry is asking for special treatment under the antitrust laws so that arrangements that might be unlawful under those laws because of their anticompetitive effect could no longer be challenged. There is no valid reason for this treatment.

The 21st amendment, which repealed Prohibition, left to the States the right to regulate the distribution of alcoholic beverages within their borders. S. 1215, rather than clarifying the States roles, as the proponents claim, intrudes the Federal Government into the States regulation of beer distribution.

Today, the question of whether or not exclusive territories should be permitted or required at the local level is determined by State legislatures and the State alcoholic beverage control commissions. However, proponents of this bill want to insure the use of exclusive territories whether or not the State actively supervises an exclusive territorial distribution scheme or even if there is no State position one way or another on the question of exclusive territories.

Proponents acknowledge that they fully intend to use S. 1215 to promote State laws and regulations requiring exclusive territories. More importantly, because enactment of S. 1215 will immunize these arrangements under the antitrust laws, exclusive territories undoubtedly will become the rule unless a State specifically prohibits them. Thus, the legislation will result in exclusive territories becoming the rule if a State does nothing one way or another on this question. In Michigan we will be stuck with this situation forever and never have a chance to repeal it.

The argument offered by proponents that this legislation is necessary because the application of the antitrust laws to beer distribution somehow violates the 21st amendment is totally wrong. Would the beer industry argue that a price-fixing conspiracy among brewers and beer distributors is legal merely because of the existence of the 21st amendment? Quite clearly, it is not the application of the antitrust laws to beer distribution that intrudes on States rights under the 21st amendment. Rather, it is the attempt by the beer industry to get the Federal Government involved in an area traditionally left to the States that does so.

If S. 1215 becomes law, the result will be exclusive territories uniformly across the Nation to the consumer's detriment, whether or not the State has approved, required or enforced that distribution system.

In conclusion, this legislation benefits absolutely no one but the special interest it is designed to protect. It will mean higher beer prices for the consumers. It guarantees that other similarly situated industries will petition Congress for their own protection.

We sincerely hope that this committee and the Congress will take the opportunity that this legislation provides to send the American public the message that we still do believe in the free enterprise system and that we still do believe in competition.

Enactment of S. 1215 will send exactly the opposite message.

We thank you for this opportunity to present our views on this very, very important subject to all of us. Thank you very much.

STATEMENT OF SENATOR ALAN SIMPSON

Senator SIMPSON. Thank you very much, Mr. Meijer. I will now relieve my good colleague from Nevada. I am Al Simpson representing the State of Wyoming in this remarkable place. I am pleased to assist in cochairing this hearing. I am happy to be here for at least a part of the testimony on this important piece of legislation.

I have a statement that I will insert into the record, without objection.

[Prepared statement by Senator Simpson follows:]

PREPARED STATEMENT BY ALAN K. SIMPSON ON S. 1215, THE MALT BEVERAGE INTERBRAND COMPETITION ACT

Thank you, Paul, for the opportunity to cochair this hearing with you. I would have wished to have been here for this entire proceeding, but I'm pleased that I could be here for at least a portion of the testimony on this important bill.

The Malt Beverage Interbrand Competition Act would clarify a potentially confusing area in the antitrust law by providing that Federal antitrust laws do not apply if a beer company sets up an exclusive territorial marketing arrangement with a beer wholesaler. These Federal antitrust laws would not apply only if there is assurance that there is substantial and effective competition from other brands within the territory. This bill deals only with Federal antitrust laws. Recognizing fully that the States have been primarily responsible for the regulation of alcoholic beverages since the repeal of prohibition, this bill would not preempt the power of any State to prohibit or permit exclusive marketing arrangements.

One of the points of any hearing is to hear all sides of an issue. To this point we've heard informative testimony from witnesses for both sides in what has been a fairly spirited debate. Let's continue this hearing by calling our next panel of witnesses.

Senator SIMPSON. Without objection, we will insert Mr. Meijer's prepared statement into the record.

[Prepared statement of Frederick Meijer follows:]

STATEMENT
# of the
FOOD MARKETING INSTITUTE

The Food Marketing Institute (FMI) appreciates the opportunity to testify in opposition to S. 1215, the Malt Beverage Interbrand Competition Act, or more accurately, the Beer Monopoly Protection Act.

FMI is a non-profit trade association whose over 1,100 members are food retailers and wholesalers of all sizes. The membership includes independent grocers, food chains, and voluntary and cooperative wholesalers. FMI's domestic member companies operate over 17,000 retail food stores with combined annual sales volume of $120 billion--half of all grocery sales in the United States. More than two-thirds of FMI's membership is comprised of independent supermarket operators or small regional firms. More than half of our retailer members are single store operators.

The Malt Beverage Interbrand Competition Act is not about competition. It's about the fear of competition. It represents an attempt by yet another industry to attain special treatment under our antitrust laws that would immunize existing firms from the vagaries of the marketplace. Under the guise of clarifying the antitrust laws, this bill will protect the profits of the beer industry to the detriment of consumers. A number of arguments are made in support of the bill. None is convincing. But the basic argument, and the least convincing, is that the beer industry _needs_ to be protected from competition. We submit that to the contrary what it really needs is a good dose of new competition.

The bill is not only unnecesary but affirmatively harmful for several reasons, which we will address in turn:

1. _The bill would decrease service and increase costs to retailers and consumers_. Exclusive territories in the beer industry have been found to _increase prices_ to consumers by _as much as 20 percent_. And make no mistake about it, the intent of, and the end result of this legislation is to promote exclusive territories in beer distribution.

2. The beer industry has not been the subject of any court decision, as the soft drink industry was, in which exclusive territories were found to be illegal under the conditions of that industry. Moreover, the beer industry already enjoys significant protection not afforded the soft drink or other industries.

3. No special circumstances render the additional protections of S. 1215 necessary. Many exclusive territorial arrangements have been sanctioned by the courts under the flexible rule of reason test applicable now to all industries. Exclusive territorial arrangements in the beer industry that are necessitated by valid business reasons and which, on balance, do not adversely affect competition or facilitate collusion are already legal and need no exemption.

4. On the other hand, the bill would insulate - in the beer industry alone - conduct that would be held to be anticompetitive under the rule of reason. Such anticompetitive practices should not be exempt from the antitrust laws.

5. The bill would interfere with state control of trade in malt beverages.

6. The precedent created by this legislation will create considerable pressure for Congress to carve out additional exemptions from the antitrust laws for other suppliers of food and grocery products.

In short, FMI opposes this legislation because it is anticompetitive, inflationary, and unnecessary. We believe that it would be especially inappropriate for the Congress to enact this protective, special interest legislation now when the virtue of free competition is being stressed in other sectors of the economy. If this bill becomes law, the only winners will be the beer distributors who will no longer have to worry about competition. The losers will be America's beer drinkers and all those who believe in free competition in the marketplace.

Exclusive Territories Mean Higher Prices and Decreased Service

In effect, S. 1215 endorses monopolies for beer wholesalers. If enacted, this legislation would allow a brewer of a particular brand of beer to enter, without fear of the antitrust laws, into an agreement with a wholesaler giving that wholesaler the exclusive right to sell that brand in the territory. Under these arrangements, retailers in the territory have to buy that brand only from the designated wholesaler. As a result, retailers and their customers are placed at the mercy of the designated monopolist. Inevitably this means higher prices for beer drinkers. Experience has proven this to be true. In Indiana, for example, a state legislative study commission recently determined that the retail price of beer went down 20 percent when that state's law was changed to prohibit exclusive territories and to allow competition among beer distributors. Since almost $10 billion was spent for beer in food and grocery stores in 1980 (70 percent of all off premises beer consumption), it is obvious that our customers have a lot to lose if this bill becomes law.

Since the retailer has no alternative supplier for the product, exclusive territories diminish the incentive for wholesalers to provide good service and competitive prices to the retailer. But it is the consumer who bears the burden of these monopolies.

The situation is analogous to you as a grocery store customer being able to shop at only one designated store in your area. Imagine if your local grocer were the exclusive distributor of food and grocery products in your neighborhood. Imagine further that a grocer outside your neighborhood is not allowed to sell to you even if you arrive at his store with cash in hand.

What could you do if you are unhappy with the local store's hours? What if the quality of the meat or produce is not acceptable? What if the store's prices are outrageously high? The short answer is that you could do nothing. Now imagine that there is a competing grocer across the street (as is probably the case in reality). In which situation do you think the local grocer will be more responsive to your needs and more competitive in his prices?

Quite clearly a law protecting neighborhood food retailers from new competition would make life easy for these grocers with guaranteed markets. But you and all the shoppers in those neighborhoods would suffer. The beer industry is asking for just that kind of protection.

Exclusive Territories Are Not Necessary to Insure Product Quality

Wholesalers and brewers argue that because malt beverages have a relatively short shelf-life, exclusive territories are needed to insure customer service and protect product quality. This argument is pure nonsense. The shelf life of most beer falls within a range of seventy-five to one hundred and twenty days. This is not a short shelf-life compared to other commodities in grocery stores. Beer is not even a perishable product as that term is defined in our industry. Grocers are used to working with truly perishable commodities such as fresh fruit and vegetables, milk, bread and meat, with far shorter shelf-lives of one to two weeks. Food store operators are, of course, quite concerned that all the products on their shelves are of good quality and will meet the demands of their customers.

Accordingly, as a matter of good and standard business practice, they institute inventory control and stock rotation procedures to assure good food sanitation and quality. The industry is proud of its record in this area. We simply do not accept the argument that it takes exclusive territories to insure fresh product. If it does, then milk, egg, produce and cookie distributors, among others, all should be included in this legislation.

Indeed, exclusive territories have the opposite effect because the lack of competition limits the wholesalers' incentive to provide a quality service. Why should the wholesaler be concerned about freshness of product or out of stocks when he has a captive customer? This service problem is especially acute for the smaller retailer who is at the mercy of one supplier. If the one monopoly distributor is more interested in serving his larger customers, there is absolutely nothing the smaller retailer can do to obtain product. If the retailer's shelves are empty and the distributor can't or won't make a delivery, there's absolutely nothing the retailer can do about that.

The bottom line is that competition does more to promote product quality and good service than anything else. To argue otherwise is to ignore reality. Retailers who operate in those states with exclusive territories as well as open states know for a fact that where monopolies exist, deliveries are more often irregular or incorrect. Shortages are more likely to occur because the one authorized wholesaler has little incentive to respond to special orders or unusual situations. Where competition exists, on the other hand, wholesalers more readily respond to special situations and deliveries generally are more timely. Product quality is certainly no better where exclusive territories now exist.

In other words, where there are alternative suppliers, it is important for the wholesaler to treat the retailer in the same manner as the retailer treats his customer. Both know that if they don't compete, they will lose their customers.

The Beer Industry Differs from the Soft Drink Industry

In a large sense this legislation seems to be a "me too" proposition. The argument boils down to "if the soft-drink industry received an exemption from the antitrust laws, why can't we?" There are, however, important differences between the two industries, their distribution systems and their legal situations. Whatever you think of the merits of the exemption for the soft-drink industry, it is important to understand these differences.

Exclusive territorial franchises have been the standard, uniform nationwide practice in the soft-drink industry for some eighty years. Among other things, that means that there has been some time for the antitrust enforcement agencies to analyze the competitive effect of that industries' distribution system. That uniform, nationwide system was directly threatened by the Federal Trade Commission when that agency issued a final decision concluding specifically that exclusive franchises as they exist in the soft-drink industry, are anticompetitive and in violation of our antitrust laws. If that decision had been upheld by the federal courts, the soft-drink industry would have had to change its distribution system. Before that could happen, Congress intervened and passed the Soft-Drink Interbrand Competition Act which averted this imminent threat to the established distribution system in the soft drink industry.

The FTC decision determined the legality of exclusive territories only as they are used in the soft drink industry. It had no effect on other industries, and other industries including the beer industry remain free to employ them until or unless they are found to harm competition substantially.

The legislative history of the soft drink bill makes it quite clear that the soft-drink legislation was premised on the very special situation facing the soft-drink industry and in no way should be considered as a precedent for other industries seeking exemption from the antitrust laws. Opponents of that bill argued it would indeed set a dangerous precedent. The proponents of S. 1215 are using it as just such a precedent. The malt beverage industry, however, is very different from the soft-drink industry.

In the soft drink industry, the syrup manufacturers sell the syrup to the bottlers who add carbonated water and then bottle the product. The bottlers in turn sell the product to the retailers.

This means that, unlike beer distributors, the soft drink bottlers are not simply middlemen or wholesalers. They add value to the product and they incur additional capital expenses to perform the processing function. These functions may well justify giving the bottlers an exclusive territory, to encourage the taking on of the necessary expense.

Beer distributors, however, are simply wholesalers or middle men, essentially no different from the wholesaler of any other product in the grocery store. They perform no manufacturing or processing function and accordingly do not have the additional capital needs of the soft-drink bottlers.

In fact, beer wholesalers do not have large capital needs relative to other industries or even to other "pure" wholesalers. For example, the general food wholesalers and self-wholesaling retailers, who warehouse and distribute thousands of different products to hundreds of different retail outlets face a much more demanding situation in terms of their physical plant, distribution equipment and capital needs. These substantial capital investments are made quite willingly even though the wholesalers are not guaranteed a monopoly in their marketing area. It is absurd to argue that beer wholesalers need such a guarantee.

A related argument in favor of vertical restraints such as exclusive territories, but equally irrelevant to the malt beverage industry, is that without the restraint on competition, distributors might not only be unwilling to make the capital investment necessary to enter the business, but they would also be unwilling to provide valuable customer services. They might be reluctant to make this investment and provide these services because competitors would gain a "free ride".

The free rider argument does not hold up under close examination. As previously discussed, beer wholesalers do not have large capital expenses. There are already significant barriers to entry so that beer wholesaling is a reasonably attractive investment for those in a position to obtain a license. In addition, the industry is quite mature and there is no substantial requirement that the distributor expend resources to attract consumer acceptance to an unfamiliar product.

The free-rider effect is pertinent if a particular distributor is required to invest considerable sums to develop a favorable consumer attitude toward the product. It might be unfair for a neighboring competitor to benefit from such expenditures by selling in the first distributor's territory. But the fact of the matter is that beer wholesalers have a built-in market. The advertising they do does not play an important role in developing a demand for the product. Brewers spend a great deal on promotion in order to create a strong consumer identification with their brands. For example, Anheuser Busch spent $180 million on advertising in 1980 and Jos. Schlitz Brewing's ad dollars totalled $66 million in that year, according to Advertising Age. We are all quite familiar with the national media advertising done by brewers. Nor do distributors do any significant price advertising. Rather, it is the retailer who is competing for the consumers business who does the bulk of retail price advertising. Distributors are the beneficiaries of all this advertising, not the creators.

In sum, in the beer industry distributors do not have large capital expenses, product quality is not a major problem, advertising and promotion is not dependent on distributor expenditures, and manufacturers (brewers) do spend extraordinarily large amounts to create a demand for their product. As a result exclusive territories simply provide a free ride to the designated monopolist. They are not necessary to protect the wholesaler from competition.

Finally, unlike the situation in the soft-drink industry, there is no uniform nationwide distribution system for beer. The states regulate the distribution of alcoholic beverages and these distribution schemes vary from state to state. The use of exclusive territories varies similarly, with some states allowing or requiring exclusive territories and others not. Thus no legal decision could threaten the kind of disruption that was facing the soft-drink industry. And, in fact, there is no pending case at the FTC or in the federal or state courts or anywhere that would mean the end of all exclusive territories in the malt beverage industry.

Thus, enactment of this legislation is not necessary to protect beer distributors. It will only upset the status quo in beer distribution, while the soft-drink legislation was necessary to preserve the status quo in that industry.

Existing Protection For Beer Distributors Means Diminished Competition

Perhaps the most important difference between the two industries in the context of this legislation is the existence of the three tier system of distribution for malt beverages which gives the beer distribution a degree of protection that is unique. In the soft-drink industry local bottlers potentially face two difficult competitive situations because of the possible vertical integration of the distribution system that would squeeze them out of the market. For example, syrup makers may own the local bottler, and they often do, or they may sell directly to the retailer and bypass the local bottler. Retailers similarly have the potential option of backward integration, that is control or ownership of the bottler or even, potentially, of the supplier itself. Thus exclusive territories may help the local bottler preserve its place in the distribution system.

But under the three tier system of distribution, vertical integration is simply not possible in the beer distribution industry. Under this system, in those states where the state has not itself taken over the distribution function, vertical integration between the manufacturer, wholesaler and retailer is generally prohibited. This means that state laws or regulations require the maintenance of three totally independent levels of distribution. The brewer may not sell directly to the retailer. But, rather the brewer must sell to an independent wholesaler who in turn sells to a non-affiliated retailer. In other words, the wholesaler is guaranteed a spot on the distribution system, free of much of the competition that wholesalers of other products face.

The retailer cannot bypass the wholesaler and buy directly from the brewer. Thus, any argument that exclusive territories are necessary to preserve the existence of the wholesaler is totally without merit. The three tier system already protects the wholesaler from new competitive approaches to distribution, approaches that may very well be more efficient than existing distribution methods. Exclusive territories go beyond that and protect the wholesaler from competition from other wholesalers. There is no valid reason to provide this additional protection.

Beer distributors are protected in other significant ways from competition. State regulations impose strict licensing requirements at all levels of beer distribution, including wholesaling. Thus wholesalers must be licensed by the state alcoholic beverage commission before being allowed entry into the marketplace. These licensing requirements vary from state to state, but they all make it difficult, if not impossible, for new competitors to enter the market. While there may be valid reasons for these licensing requirements, their effect is to establish barriers to new competitors and to diminish the amount of competition in the industry. In addition, states have laws or regulations limiting price competition in a variety of ways. For example, some states require price posting or price affirmation, others prohibit volume discounts. The result is an industry that already is less competitive in significant ways than most other unregulated industries.

Current Law Offers Adequate Protection for Lawful Activity

Proponents of S. 1215 argue that beer distributors need the special protection offered by this legislation because present law threatens distribution arrangements. In fact, the state of the law is such that there is simply no need for this legislation. As previously noted, beer distributors already have special protection not available to most other industries; that makes the beer industry an especially inappropriate one to warrant this additional special treatment under our antitrust laws.

Attached to this statement is a legal analysis of this bill which explains the law of exclusive territories generally and as it applies to the beer industry specifically. In summary, vertical restraints, such as exclusive territories are not *per se* lawful or unlawful. They are judged under what is known as the rule of reason. Under this flexible approach, a court must determine, based on the circumstances of each case, whether the vertical restraint on trade is supported by valid economic reasons for the restraint, and whether the anti-competitive impact is outweighed by other pro-competitive aspects. Courts have had no difficulty in applying this standard to arrangements providing for exclusive territories. In many cases courts have upheld these arrangements as pro-competitive. Brewers at present can and do enter into exclusive territorial arrangements with wholesalers, and some of those arrangements have been upheld by the courts. Thus the law in this area is clear and it causes no special problems for beer distributors.

The Bill Could Immunize Anitcompetitive Activity

With this legislation, the beer industry is asking for special treatment under the antitrust laws so that arrangements that might be unlawful under those laws because of their anticompetitive effect could no longer be challenged. There is no valid reason for this treatment.

S. 1215 would create a weaker standard for judging exclusive territorial arrangements in the beer industry by making such arrangements immune from prosecution as long as "substantial and effective" interbrand competition exists. Under the rule of reason, the existence of interbrand competition is just one factor to be considered in looking at the lawfulness of the restraint. It is not determinative of the issue. And it should not be. The nature of the restraint and its effect, the history of the restraint, the reason for adopting the particular restraint and the purpose sought to be attained are all relevant facts. An extremely important factor in any rule of reason determination is whether or not the restraint is broader than necessary to accomplish the purpose. Perhaps primary areas of responsibility, rather than exclusive territories, provide all the protection necessary to beer distributors. If product quality is the issue, perhaps open dating is the answer. S. 1215 eliminates all these considerations from the equation.

Moreover, the legislation does not define what "substantial and effective interbrand competition" is. Proponents apparantly believe that it is merely that competition which currently exists in the beer industry, or that which would exist whenever two different brands of beer are available to consumers. We believe that substantial and effective competition does not exist today in the beer industry. Without further definition of this term, S. 1215 might create more confusion and disparity of treatment than ever under the antitrust laws.

Because of the high concentration in the beer industry, the Department of Justice has concluded that the proposed weaker standard for judging exclusive territorial arrangements in the beer industry is especially undesirable. According to the Justice Department the beer industry is one in which the risk of anticompetitive effects from the widespread use of exclusive territories "is almost uniquely high."

In 1980 the top two brewers had a combined national market share of 50 percent and the top four had over 67 percent. The top six brewers controlled 83 percent of the market. And more mergers seem to be occuring daily, further increasing concentration.

At the state level, this concentration is even higher, with four firm sales concentration exceeding 80 per cent in 30 of 39 states in which information was available, according to the Justice Department. This concentration is even higher at the wholesale level because of the use of exclusive territories, or primary areas of responsibility. In addition, many wholesalers distribute the brands of more than one brewer. So even though there may, for example, be four brewers "competing" in a market, there may be only two wholesalers distributing the product. As a result there is, in fact, a surprising concentration at the wholesale level where sixteen percent of the wholesalers control 55% of the national market.

Twenty-First Amendment and States Rights

The twenty-first amendment, which repealed prohibition, left to the states the right to regulate the distribution of alcoholic beverages within their borders. The states do have wide latitude in the area of liquor distribution and they have exercized their authority in this area by establishing a wide variety of laws and regulations concerning the distribution of alcoholic beverages.

S. 1215 introduces the federal government into this area of state regulation by endorsing a particular system of beer distribution. It will in a subtle but significant way intrude into the states regulation of beer distribution. Today, the question of whether or not exclusive territories should be permitted or required at the local level is determined by the state legislatures or the state alcoholic beverage control commissions.

If the state has a clearly articulated or affirmatively expressed policy requiring exclusive or other restrictive arrangements which it actively supervises or implements, those arrangements are shielded from the antitrust laws by the state action doctrine.

However, proponents of this bill are not defenders of state's rights. They want to insure the use of exclusive territories whether or not the state actively supervises an exclusive territorial distribution scheme or even if there is no state position one way or the other on the question of exclusive territories.

Proponents of this legislation acknowledge that they fully intend to use S. 1215 to promote state laws and regulations requiring exclusive territories. More importantly, because enactment of S.1215 will immunize these arrangements under the antitrust laws, exclusive territories undoubtedly will become the rule unless a state specifically prohibits them. Thus this legislation will result in exclusive territories becoming the rule if a state does notning one way or the other on this question.

The argument offered by proponents that this legislation is necessary because the application of the antritrust laws to beer distribution somehow violates the twenty-first amendment is totally specious. Would the beer industry argue that a price-fixing conspiracy among brewers and beer distributors is legal merely because of the existence of the twenty-first amendment? That amendment does give the state wide latitude to regulate liquor distribution, but the regulation must be in aid of an important state interest, clearly espoused and carefully monitored by the state.

When federal principles embodied by the amendment and the antitrust laws clash, it is well settled that the antitrust laws may take precedence. In fact, the Supreme Court has recently held that a state law requiring a retail price maintenance scheme by the liquor industry in California did violate the antitrust laws. And properly so, because as the Court said there, the "Twenty-First Amendment provides no shelter from a violation of the Sherman Act."

Quite clearly, it is not the application of the antitrust laws to beer distribution that intrudes on states rights under the twenty-first amendment; rather, it is the attempt by the beer industy to get the federal government involved in an area traditionally left to the states that does so. If S. 1215 becomes law, the federal government will be sending a clear message to the states, to the industry and to consumers. The result will be exclusive territories uniformly across the nation to the consumer's detriment, whether or not the state has approved, required or enforced that distribution system.

Legislation Will Create a Dangerous Precedent

The precedent created by this legislation will create great pressure for Congress to extend similar protection to suppliers of other food and grocery products. Wine distributors, for example, have already expressed interest in a similar exemption. Since beer distributors are essentially no different from wholesalers of any other product in the grocery store, it will be hard to justify not extending this protection. Thus the impact of this legislation may very well spread far beyond the beer industry.

Competition Promotes the Public Good

As noted previously, FMI and its members believe strongly in competition. We believe that competition promotes efficiency and benefits consumers. There is no doubt that exclusive territories for beer distributors mean higher prices for consumers. As noted, prices went down in Indiana by over 20 percent when territories were opened up. This should not be a surprising fact. The antitrust laws, after all, are based on the premise that competition promotes the public good and that monopolies and the profits associated with them do not contribute to the long-term economic health of our society. That is why those seeking special treatment under the antitrust laws should bear a very heavy burden to show a compelling need for such treatment.

As we have already demonstrated, the beer industry is already one with limited competition because of high concentration and heavy regulation. We would suggest that what that industy needs is more competition, not less. Beer wholesalers who are already protected from competition by the three tier system of distribution now seek to be immune from even the hint of competition from other beer wholesalers. They argue in essence that some beer wholesalers might grow larger than others and the smaller ones might not be able to compete with them. This argument rests on several questionable assumptions. The first being that small entities cannot compete effectively with larger ones unless they have guaranteed territories. The fact is that local wholesalers often have significant competitive advantages over larger competitors. They are, of course, closer to their customers. This means significant advantages in transportation costs. In addition, local wholesalers have built up substantial good will with their customers over the years and, therefore, should understand their market better than outsiders and should be closer to their customers needs. In other words, it is the efficient firm that will survive and prosper, not necessarily the larger one. Smaller firms are not necessarily inefficient.

Among food retailers, for example, independent grocers, in the last several years, have been more profitable on the average than the chains according to industry research. Also, contrary to the claims of proponents of this legislation, concentration among retailers is not increasing. A recent study by a professor at Washington State University shows that the total number of retail outlets has declined over the years as store sizes have increased. But, over the last decade retail food chains' share of total grocery sales and stores has decreased. This may very well be because the independent grocer is closer to his customer and has learned to compete effectively for the consumer's business.

This legislation in reality seals the fate of the beer distributor it is supposed to protect. Small efficient bottlers will be locked into their territories and will have no chance to expand into new markets and to develop more efficient marketing and distribution techniques. Concentration will increase as small distributors with their guaranteed little markets will become more attractive acquisition targets. Investors will buy them out in order to acquire larger territories. This is exactly what is happening in the soft drink industry. Perhaps this is the true attraction of this legislation to the beer barons. It will allow them to capture the value of their monopolies when larger consumers, pay premium prices for the acquisition of these exclusive territories.

In conclusion, this legislation is totally without any redeeming value. It is unnecessary. It benefits absolutely no one but the special interest it is designed to protect. It will mean higher beer prices for consumers. And it guarantees that other similarly situated industries will petition Congress for their own protection.

We sincerely hope that this committee and the Congress will take the opportunity that this legislation provides to send the American public the message that we still do believe in free enterprise and competition. Enactment of S. 1215 will send exactly the opposite message.

We thank you for the opportunity to present our views on this important subject.

ATTACHMENT

LEGAL ANALYSIS OF THE MALT BEVERAGE INTERBRAND COMPETITION ACT ("MALT BEVERAGE ACT")
S. 1215 and H.R. 3269

Currently pending in the House and Senate Judiciary Committees are identical bills, H.R. 3269 and S. 1215, each denominated "Malt Beverage Interbrand Competition Act" (hereinafter "Malt Beverage Act"). The Malt Beverage Act would grant the brewing industry a special exemption from federal antitrust laws by permitting brewers to enter into exclusive territorial agreements with wholesale distributors provided there is "substantial and effective competition" in the geographic area affected by the agreement. Although the stated purpose of the bill is to "clarify existing law regarding territorial provisions,"1/ this legislation in fact significantly alters existing law and creates special unjustified antitrust immunity for a single industry.

Proponents of the Malt Beverage Act assert that the pending legislation is needed (1) to provide legal certainty in this area of antitrust law and to avoid litigation allegedly fostered by the present standard; (2) to confirm the regulatory power of the States; and (3) to reduce costs to consumers. These alleged justifications are unpersuasive. The proposed bill is unnecessary at best, and seriously anticompetitive at worst.

1/ H.R. 3269, 97th Cong., 1st. Sess. (1981).

1. Present Law Regarding Exclusive Territories Provides the Optimal Balance of Legal Certainty and Flexibility Necessary to Implement the Goals of Federal Antitrust Law.

A. The Bill Would Alter Present Law

The prevailing legal standard applicable to vertical, non-price[2] restraints, including exclusive territorial agreements, was established by the Supreme Court in Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977). In that case the Court rejected its previously adopted *per se* prohibition against such agreements[3] in favor of the more flexible "rule of reason" approach. Under the rule of reason courts must determine whether, under the particular circumstances of a case, a given restriction constitutes, on balance, a reasonable or unreasonable restraint of trade. As stated by Justice Brandeis in Chicago Board of Trade v. United States, 246 U.S. 231 (1918), "the true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition, or whether it is such as may suppress or even destroy competition." *Id.* at 238.

Finding the rule of reason appropriate to apply in *Sylvania*, the Court reasoned that under certain competitive conditions vertical restraints may enhance competition more than they restrict it. For example, an arrangement that reduces or eliminates intrabrand competition might have the desirable effect of introducing or enhancing interbrand competition, so that competition is, on balance, increased.

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[2] There is a considerable body of legal opinion which suggests that at least some price related vertical restraints, such as maximum resale price maintenance, should also be judged by the same "rule of reason" applied to non-price vertical restraints. This view has not yet been adopted by the Supreme Court.

[3] United States v. Arnold, Schwinn & Co., 388 U.S. 365 (1977).

In determining whether a restraint is reasonable, the courts generally consider whether the restraint (1) is reasonably necessary to the legitimate primary purpose of the arrangement, and of no broader scope than reasonably necessary; (2) does not unreasonably affect competition in the market place; and (3) is not imposed by a party or parties with monopoly power. United States v. Columbia Pictures Corp., 189 F.Supp. 153, 178 (S.D.N.Y. 1960). In short, the rule is comprehensive and flexible, susceptible of application to many competitive situations, and capable of incorporating a wide range of competitive factors.

Although, in discussing the application of the rule of reason to the exclusive territory agreements at issue in Sylvania, the Supreme Court noted that interbrand competition is of primary concern of antitrust laws, it did not suggest that the mere existence of interbrand competition in a market justifies the elimination of intrabrand competition. Rather, a finding of reasonableness requires that the restraint increase interbrand competition more than it lessens intrabrand competition. Reasonableness under current law also depends on a showing that the restraint is not otherwise likely to have anticompetitive effects. In contrast the Malt Beverage Act would appear to countenance the total elimination — not merely the reduction — of intrabrand competition, provided only that there be some interbrand competition in the marketplace.

Thus, rather than "confirm and clarify" the comprehensive rule of reason adopted in Sylvania, the proposed legislation would alter present law by focusing exclusively on the existence of interbrand competition. The approach embodied in the Malt Beverage Act makes no attempt to employ a balancing test or to assess likely procompetitive and anticompetitive effects of territorial restraints in a given market. Vertical restraints may not only decrease intrabrand competition, but may have other horizontal anticompetitive effects as well. For example, in a market where several manufacturers employ similar vertical restraints, the ability to collude — by means of price fixing, territorial allocation, and other per se illegal schemes — is necessarily greatly enhanced. The rule of reason permits the courts to take into account the likelihood that such anticompetitive effects would flow from a vertical restraint; the proposed legislation would not.[4]

Moreover, by indiscriminately authorizing exclusive agreements which impose an absolute prohibition on sales outside a geographic area, the bill would discourage manufacturers from using less restrictive marketing schemes, such as areas of primary responsibility, which promote interbrand competition but do not wholly eliminate intrabrand competition.[5]

B. The Purported Need for Legal Certainty Does Not Justify Altering Present Law.

As demonstrated above, the proposed bill does not, as its sponsors assert, "merely clarify existing law." Equally faulty is the sponsors' contention that legal certainty, i.e., a rule of "per se" legality, in the area of territorial restraints is either desirable, in general, or necessary with respect to the malt beverage industry. The lower courts have shown no reluctance to apply the ruling in Sylvania to vertical restraints, including territorial restraints, in a variety of industries. Analogies to the arguments advanced last year by proponents of the Soft Drink Interbrand Competition Act, moreover, are faulty. By that Act, Congress exempted the soft drink industry from antitrust laws applicable to territorial restraints. The Soft Drink Bill was introduced largely in response to a ruling by the Federal Trade Commission that the use of exclusive territories for bottlers and distributors was illegal under the market conditions of that industry.[6] Proponents of the bill convinced Congress that legislation was necessary to avoid the purported "confusion" created by the FTC's decision, which the sponsors argued was inconsistent with the courts' more tolerant view of territorial restraints under the rule of reason. Whatever may have been the merit of the claimed need for special legislative clarification in the soft drink industry, there is no evidence of confusion regarding the rule of reason as it is currently applied to territorial restraints in other industries, including the malt beverage industry. The only "confusion" that may exist now concerns which industry will line up next for its exemption from the antitrust laws. Moreover, it should be noted that if the "substantial and effective competition" precondition in the instant legislation is meant to be a real condition precedent, it is so vague that it is likely to engender more litigation than the legislation it is supposedly designed to forestall.

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[4] In at least one recent case vertical restrictions have been successfully challenged as ancillary to a price-fixing scheme and were held illegal per se. Pitchford Scientific Instruments Corp. v. PEPI, Inc., 440 F.Supp. 1175 (W.D.Pa. 1977), aff'd without published opinion, 582 F.2d 1275 (3rd Cir. 1978), cert. denied, 440 U.S. 981 (1979).

[5] As one respected antitrust scholar critical of the use of exclusive territorial agreements noted, "almost all imaginable legitimate business reasons can be achieved by more moderate vertical restrictions or alternative techniques that involve no intra-brand restrictions at all." Pitofsky, "The Sylvania Case: Antitrust Analysis of Non-Price Vertical Restrictions," 78 Columbia Law Review 1, 22, 28 (1978).

In any event, the Supreme Court's rejection in Sylvania of its prior per se rule against exclusive territorial agreements reflects a determination that legal certainty is not the paramount value in the area of trade regulation. The Sylvania Court noted that the advantages of *per se* rules in tending to provide guidance to the business community and to minimize burdens on litigants and the judicial system "are not sufficient in themselves to justify the creation of per se rules." (emphasis added) Sylvania, at 50 n. 16. This reasoning should apply with even greater force against the proposed legislation which would effectively create a *per se* rule immunizing a single industry from antitrust laws for the sake of certainty and efficiency. Just two years ago the National Commission to Review Antitrust Laws and Procedures concluded that proponents of any form of antitrust immunity should have the burden of overcoming a strong presumption against special protection by clear and convincing factual evidence that characteristics of a particular industry make the application of usual antitrust standards unwarranted.[7] The purported need to replace the present flexible rule with a fixed legislative immunity in the interest of clarity and legal certainty falls far short of the type of "compelling reason" envisioned by the National Commission.

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[6] The Coca-Cola Co., 91 FTC 607 (1978).

2. The Proposed Bill Is Not Necessary to Confirm the Power of States to Regulate the Importation and Distribution of Alcoholic Beverages

Proponents of the Malt Beverage Act argue that recent Supreme Court and state court decisions defining the limits of states' powers under the Twenty-first Amendment indicate the need for legislation exempting the brewing industry from antitrust laws. However, examination of the most recent decision of the Supreme Court in this area and related state court decisions reveals that congressional action is not needed to reinforce the Twenty-first Amendment or to clarify present law.

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[7] Report of the National Commission for Review of Antitrust Laws and Procedures, 186-87 (1979).

Last year in California Retail Liquor Dealers Association v. Midcal Aluminum, Inc., 445 U.S. 97, 100 S.Ct. 937 (1980), the Supreme Court held that state laws imposing a retail price maintenance scheme on the liquor industry in California violated antitrust laws. The Court concluded that neither the Twenty-first Amendment[8/] nor the "state action" doctrine[9/] immunized the challenged law from antitrust attack.

In reaching this conclusion, the Court reviewed its earlier decisions that establish that, although the Twenty-first Amendment gives states wide latitude in the area of liquor regulation, there are important federal interests which have survived the ratification of the Twenty-first Amendment. Midcal, supra, 100 S.Ct. at 945. Examples of prior cases identifying such important federal interests, noted by the Court, include Department of Revenue v. James Beam Co., 377 U.S. 341 (1964) (states cannot tax imported liquor in violation of the Export-Import Clause); Craig v. Boren, 429 U.S. 190 (1976) (states cannot establish sex-based minimum ages for purchase of beer in violation of Equal Protection Clause); Hostetter

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[8/] Section 2 of the Twenty-first Amendment reserves to the States certain powers to regulate the liquor industry: "The transportation or importation into any State, Territory or possession of the United States for delivery or use therein, in violation of the laws thereof, is hereby prohibited."

[9/] Under the "state action immunity" doctrine in Parker v. Brown, 317 U.S. 341 (1943), a regulatory scheme cannot violate the Sherman Act if that scheme meets two criteria: (i) the challenged restraint must be "one clearly articulated and affirmatively expressed as state policy "and (ii) the regulatory policy must be "actively supervised" or implemented by the State. In Midcal the Court ruled that the retail price maintenance policy in California met the first requirement of the state action immunity doctrine, but failed the second because the state did not implement or monitor the challenged pricing system.

v. Idlewild Liquor Corp., 377 U.S. 324 (1964) (states' power to regulate liquor distribution remains subject to Commerce Clause). The Midcal Court stressed that in cases involving the Twenty-first Amendment "competing state and federal interests can be reconciled only after careful scrutiny of those concerns in a 'concrete case'." 100 S.Ct. at 946. When the Court compared the important policies embodied in the Sherman Act's prohibition against price-fixing with the relatively weak justifications offered in support of the state's price maintenance scheme, it concluded that "the asserted state interests are less substantial than the national policy in favor of competition." Id. at 947. Although the Court held that the Twenty-first Amendment did not immunize California's price maintenance scheme from the reach of the Sherman Act, Midcal should be read as a recognition of the states' broad powers under the Twenty-first Amendment when an important state regulatory interest is at stake. The Midcal Court explicitly reserved the question "whether the legitimate state interests in temperance and protection of small retailers could ever prevail against the undoubted federal interest in a competitive economy." Id. at 947.

The question reserved in Midcal was the subject of a Kansas Supreme Court decision reached two months prior to the Midcal opinion. In Colby Distributing Co., Inc. v. Lennen, 227 Kan. 179, 606 P.2d 102, appeal dismissed sub nom. Grant-Billingsley Liquor Co. v. Lennen, 101 S.Ct. 342 (1980), the Kansas court upheld a state law that imposed extensive control over intra-brand competition by permitting the use of exclusive territories in order to strengthen interbrand competition among distributors. The state court's decision was based on an exhaustive review of the state's prohibitionist history and the important regulatory objectives of the challenged law. The court accepted the state's purposes promoting temperance by monitoring the flow of liquor and "introducing competitive pricing into the middle tier of the Kansas liquor distribution system" — as a proper objective within the Twenty-first Amendment. 606 P.2d at 111.

Despite suggestions to the contrary, there is no inconsistency between the Supreme Court's treatment of Midcal and Colby, since the latter case involved the type of non-price restraints enacted for legitimate regulatory purposes that the Midcal court suggested might be protected by the Twenty-first Amendment. An appeal from the Colby decision was summarily dismissed by the United States Supreme Court on the basis that no substantial federal question was presented. Thus the Supreme Court apparently did not view Colby as inconsistent with its Midcal decision. Grant-Billingsley v. Lennon, supra. And it should be emphasized that by dismissing the Colby appeal, the Supreme Court let stand the Kansas state law permitting exclusive territorial franchises.

Proponents of the Malt Beverage Act point to a recent decision of the California Court of Appeals, Norman Williams Co. v. Rice, No. 80-1012 cert. granted; 50 U.S.L.W. 3447 (December 12, 1981), argued (April 21, 1982), as an indication that the states' Twenty-first Amendment rights need legislative clarification and reinforcement and as a justification for this legislation. In Norman Williams a California appellate court held that the state's "primary source" or "designation" statute violated federal antitrust laws and was not protected by the Twenty-first Amendment or the state-action exception to the antitrust laws. Primary source or designation laws prohibit any licensed importer from importing branded liquor unless he is authorized to do so by the brand owner or distiller. Under normal competitive conditions, these laws may be considerably more restrictive of competition than the exclusive territorial agreements which the Malt

Beverage Act would sanction. Whereas that Act would permit the use of exclusive agreements voluntarily entered into by brewers and their chosen distributors, primary source laws permit an individual brewer to forbid third party retailers, unrelated to the agreement, to import a given brand even from an independent source. Unless every wholesaler in every state is bound by exclusive territorial agreements, the Act would have a less restrictive effect than a "primary source" law. Accordingly, the Norman Williams, Midcal and Colby decisions are not necessarily inconsistent and do not indicate that present law is confused or that the states' regulatory powers are threatened.

In Colby the Kansas state court found that the state legislature had enacted a law permitting exclusive franchises in order to cure market defects peculiar to the liquor industry in Kansas. By contrast, in Norman Williams, the California state court found no legitimate regulatory interest reflected in the state's original source laws. As noted in the Brief in Opposition to Petition for Certiorari in the Norman Williams case, it is not surprising that a court in Kansas — where the liquor industry has been influenced by a strong prohibitionist tradition and the lowest per capita consumption of alcohol in the nation — would reach a conclusion regarding the legitimacy of state interest in regulation different from that of a court in California where the per capita consumption is high.[10/] Rather than exhibiting confusion in the application of antitrust laws under either Sylvania or Midcal, these two state court decisions reflect the flexibility the Supreme Court meant to preserve in Midcal by adopting a case by case approach that requires balancing of the federal interest in preserving competition against the regulatory interests of each state.

[10/] Consolidated Brief in Opposition to Petitions for Certiorari, Rice v. Norman Williams Co., pp. 22-24.

Significantly, the Malt Beverage Act even if enacted into law, would not necessarily affect the decision in Norman Williams which concerns the more restrictive primary source laws. By citing the Norman Williams decision as justification for this legislation, proponents are, in essence, arguing that the beer industry should be totally exempt from the antitrust laws. The long line of cases previously cited in the Midcal decision indicates that this argument is wholly without merit. As the Supreme Court explained in Midcal, it is well established that "the Twenty-first Amendment provides no shelter from the violation of the Sherman Act."

3. The Proposed Bill Will Promote a Less Competitive Beer Industry

If the Malt Beverage Act is passed, Congress will be endorsing exclusive territorial monopolies for beer distributors. Retailers will confront a distribution system that will require them to purchase each brand of beer from a single source. This scheme will eliminate the intrabrand competition among distributors which might otherwise permit retailers to buy and sell malt beverages at lower cost to consumers.

Interbrand competition in the malt beverages industry is already at a minimum because small regional brewers have been forced out of business in recent years. Presently, the top six brewers account for 83% of all domestic beer sales. The elimination of intrabrand competition under these circumstances would have particularly adverse effects in the malt beverage industry. This is so because brand loyalties of consumers of malt products is generally very strong. The malt beverage market, like other relatively concentrated industries, may well be less sensitive to interbrand price competition than many other product markets, so that intrabrand price competition must play a correspondingly larger role in establishing a competitive resale price.[11] These market factors, peculiar to the malt beverage industry, suggest that the proposed law is far more likely to increase, not decrease, costs to consumers.

Conclusion

As the preceding discussion indicates, the justifications offered by proponents of the Malt Beverages Act lack merit. The present "rule of reason" approach to exclusive territorial restraints provides adequate legal certainty and preserves the flexibility necessary to implement the goals of antitrust law. Under the Twenty-first Amendment, as interpreted by recent Supreme Court decisions, states retain their power to regulate the importation and distribution of alcoholic beverages pursuant to a legitimate regulatory goal. They are not free, however, to violate federal antitrust law by imposing price-fixing schemes. The present case-by-case approach, which requires an assessment of all the market effects of a particular territorial scheme, eliminates only those arrangements which unreasonably restrict retailers' ability to obtain and sell malt beverages at the most competitive prices. For these reasons the proposed legislation exempting a single industry from present antitrust laws is both unnecessary and undesirable.

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[11] See United States v. Philadelphia National Bank, 374 U.S. 321 (1963).

Senator **Simpson**. We will continue then with the second member of this panel. Thank you, Mr. Meijer. Now we have Mr. Protos.

If we could emphasize again the necessity of following some kind of time limit here, or we will indeed find ourselves without a chairman again in an hour or so because of a previous commitment. Please limit your oral statements to 5 or 7 minutes. That would be most helpful.

Mr. **Protos**. Mr. Chairman, I will be just as brief as possible.

My name is Matthew Protos. I am here today speaking as president of the National Licensed Beverage Association in opposition to S. 1215. I appreciate the opportunity to present our views at this time.

The National Licensed Beverage Association is a nonprofit trade association with headquarters in Alexandria, Va. We offer services in public affairs, education and research to our more than 30,000 members, who operate on-premise licensed beverage retail establishments such as cocktail lounges, taverns and restaurants across the country.

At this time, Mr. Chairman, I would like to inject that I am from Montgomery County, Md., personally, the sole jurisdiction that controls malt beverages. We are the only jurisdiction in the Nation where the county government is in the beer business. I can assure you that our beer prices in Montgomery County are very substantially higher than they are in the surrounding jurisdictions of northern Virginia, Washington, D.C., and the rest of the State of Maryland.

The majority of these small businessmen have a deep concern about the consequences of S. 1215 if it becomes law. They are very worried about the detrimental effects it will have on their businesses, their livelihood, and their families.

Their concern is that neither the small businessman nor the American consuming public would be served best by granting special exemption of antitrust laws of our Nation to a self-interest group. This action would create beer barons throughout the marketplace. In fact, we view this type of legislation as harmful to the consumer and the retailer because it would put your stamp of approval on a monopolistic situation.

We are afraid that favorable recommendation by this committee and the ultimate passage of this proposed legislation will create many negative situations for which the American consuming public will pay the price.

First, granting a self-interest group special exemption to the antitrust laws will surely open pandora's box and encourage every other self-interest group to seek similar treatment. After all, a legal monopoly could be very lucrative. Already other organizations are waiting in the wings to see what action is taken on S. 1215. There is no doubt in my mind that, if the beer wholesalers receive favorable action on this legislation, the wholesalers of distilled spirits will attempt to amend the bill or will submit legislation of their own granting them the same privileges.

It is my understanding that the Sherman Antitrust Act was written to prevent large monopolies and to foster free market competition which is the cornerstone of our very successful free enterprise system. NLBA fails to see why one industry should be exempted from laws by which all other American industries must abide. If such an exemption is granted by the passage of this legislation, I am sure that other industries will seek the same special treatment. Let us not forget that antitrust laws were enacted for the protection of the small businessman and the consuming public. Special exemptions to these laws can only reverse that protection and lay open the small businessman and consuming public to the whims of what we call the beer barons who would have the exclusive rights to sell their brand of beer to retailers within the boundaries of their kingdoms. As in any feudal economy, this one too would be supported on the back of the peasants, in this case the consumer.

In reality, this has already happened. Just the year before last, Congress set a precedent by allowing the soft drink industry exemptions to antitrust. Today we have proof that others will seek this exemption. That is why we are here.

What have been the results of granting the soft drink industry this exemption? One answer is higher prices to the consumer. Since granting the exemption to the soft drink industry, prices have soared so that I now pay more for soft drinks I purchase for my restaurant than I do for beer. There is only one way I can stay in business, and that is to pass this increased cost on to the consuming public.

Granting wholesalers exemption to the antitrust laws of this country eliminates wholesale competition and places the retailer at the mercy of, in this case, the beer wholesaler. When you eliminate competition, you upset the marketplace. Eliminating competitive pricing will allow a sole wholesaler to dictate his price within his kingdom.

So a major concern with the passage of this proposed legislation by the industry retailer is the increase in cost to the consuming public. Not that it could happen, but that it will happen as we have already witnessed in the soft drink industry.

Another concern is that, if Congress approves this legislation, it will increase the pressure on many State legislatures to pass exclusive territory laws. Some States have exclusive territory laws at the present time. Whether they are legal under current antitrust laws is a matter for the Justice Department to determine. But we can illustrate the havoc they have caused retailers in the American marketplace.

This can best be explained by stating the plight of one of our members in the State of Wisconsin, which has an exclusive territory law. Let us call him Mr. Jones. Each week wholesaler A sends out his truck loaded with brand X and brand Z beers to Mr. Jones' establishment. However, wholesaler A is only allowed to sell brand X to this retailer because he did not have the territorial rights to sell brand Z at this location. Meanwhile, wholesaler B, who has territorial rights to sell brand Z, was 40 miles away from Mr. Jones' location. This required an 80-mile round trip to service Mr. Jones. Because of this additional travel, wholesaler B understandably charged more to Mr. Jones for brand A than the price wholesaler A had established for other retailers, some of whom were no more than 3 miles from Mr. Jones' establishment. Because of an exclusive territory law, Mr. Jones was forced to charge more for brand Z than his competitors within a 5-mile radius or receive less profit.

He also was forced to carry a larger inventory because wholesaler B chose to call on him only once every 2 weeks because of the distance involved. Yet, wholesaler A was at Mr. Jones' establishment every Monday morning with brand Z on his truck at a much lower price but unable to sell it to Mr. Jones because he was not in his territory. If that all sounds very confusing, you are right; it is. So, you can imagine the plight of the small retailer trying to operate his business under such circumstances.

Exclusive territorial agreements cause such situations to exist on a frequent basis and leave the retailer no choice but to pay higher prices for a brand or not to carry that brand. This brings us to product loyalty. Product loyalty is very strong and indicates how well the major breweries have done in marketing their products. In fact, it is so strong that retailers do not sell a brand so much as they sell their place as the best place to buy that brand. In our industry, intrabrand price competition plays a larger role in establishing a competitive resale price than in other industries. Thus, we have the American consumer who will end up paying the increased price rather than switching brands.

This also brings up another question of availability. If my exclusive wholesaler runs out of my customers' favorite brand or if a strike, natural disaster, such as a flood or electrical failure, prevents my wholesaler from delivery, I would be prevented from looking for another source of supply.

There are purely legal reasons why we do not need this legislation and it could be interpreted as being harmful. Our antitrust laws are flexible and meant to be that way. If the beer wholesalers were indeed an industry which needed help, it is most likely that this help could be provided within the parameters of existing law.

It should be pointed out that the 21st amendment does not shelter our industry from violation of the Sherman Antitrust Act. This fact was emphasized in a recent Supreme Court decision, *Midcal.*

The limits placed on the alcohol beverage industry are many and well documented. This industry is well regulated at both the Federal and State levels. The three-tier system of distribution regulates competition among distributors. NLBA feels that these proposed additional limits on competition in S. 1215 would help the first two levels of distribution to the detriment of the third, the retail level, the level of our members. In addition, this bill would limit competition to the detriment of the consumer, who will pick up the extra tab in the final analysis.

The proponents of this legislation would lead us to believe that their industry is threatened by transshipping and that this special waiver of the antitrust laws is needed to save the industry. Let me state that transshipping is nothing new to the beer business. It has gone on for years, often by one wholesaler within his own area. This is especially true in summer resort areas where large inventories of beer are picked up at the end of the season and dumped on other accounts which remain open throughout the year. There are laws to regulate the sale of alcohol beverages across lines of particular government jurisdictions and the disadvantages of transshipping within a designated area can best be controlled by self-regulation and self-policing within the industry.

Proponents of this legislation further state that transshipping affects the consumer because transshipped beer has often exceeded its shelf life and the consumer is sold old beer. Yet, to my knowledge only one major brewery clearly indicates the brewing date of its product on the container. Other breweries use a label code which is indistinguishable to the consuming public and to the retailer, for that matter. If stale beer is the issue here, why is not the brewing date made available and clearly marked on the containers, as is done with so many other products we purchase today? The truth of the matter is that the passage of S. 1215 will provide the wholesalers with beer baron kingdoms at the expense of both the small licensed beverage retailer and the American consuming public. The possibility of stale beer is no excuse to undermine sound law.

Fifty years ago, our country repealed the disastrous experiment of Prohibition. In doing so, we enacted strong Federal and State regulations to protect the American public as the sale of alcohol beverages once again became legal. Today, we sit here contemplating legislation that could exempt a special group from the laws that were designed to protect that same public. We do not need the rebirth of beer barons in our industry or in the American marketplace.

In summary, we believe that S. 1215, by granting special treatment under the antitrust laws, would be harmful to the small licensed beverage retailer and to the American public. We are concerned because this unnecessary proposal would tamper with the integrity of antitrust laws, would risk the future of certain small businesses, and would promote higher prices at a time when this country is fighting inflation. For these reasons, we ask that the committee defeat S. 1215. I thank you for the opportunity to comment on S. 1215, the Malt Beverage Interbrand Competition Act.

Senator SIMPSON. Thank you very much, Mr. Protos. Next we will hear from Mr. Mac Greer, president of the Alabama Retail Association, Montgomery, Ala.

Mr. GREER. Thank you, Mr. Chairman. My name is Mac Greer. I am president of the Alabama Retail Association. Our association represents thousands of food retailers across the State of Alabama who oppose S. 1215. I am also vice president of a family business founded in 1916 by my grandfather. We today operate 34 grocery stores in Alabama and Mississippi and also are fortunate enough to serve hundreds of independent grocers in Alabama and Mississippi.

This legislation provides special treatment under the antitrust laws for arrangements between brewers and beer distributors by allowing exclusive territories. It represents an attempt by the beer industry to use the Federal Government to accomplish what that industry has been unable to accomplish in the States. In Alabama, those of us who believe in competition have been fighting similar proposals in our State legislature. These anticompetitive bills would require each manufacturer or importer of alcoholic beverages to designate exclusive sales territories for each of its brands sold in Alabama and would further require them to name one exclusive wholesaler for each such sales territory. Thankfully, we have been successful in stopping this legislation which would only result in less competition and in higher costs to the consuming public.

Today, distribution of alcoholic beverages in Alabama is strictly regulated at both State and Federal levels. In our State we have a three-tier system of distribution of beer under which manufacturers, wholesalers, and retailers are kept separately and independently from each other.

By law, manufacturers must sell only to the wholesaler and the wholesaler only to the retailer. This system stringently regulates the amount of competition. But the proponents of exclusive territorial legislation wish to reduce this competition even further.

Under the proposal before you, a brewer of a particular brand of beer could lawfully enter into an agreement with a wholesaler which would grant that wholesaler the exclusive rights to that brand of beer in a particular territory. Such an arrangement would limit competition.

For a moment let us look at what is actually happening in the Alabama marketplace among wholesalers and retailers as far as beer is concerned.

Incidentally, there happens to be a couple of my good friend distributors in the back of the room right now.

Most retailers in Alabama deal with a local beer distributor who serves the territory where the store is located. Retailers and local distributors have had beneficial dealings with each other over the years. The distributors generally understand and provide the services needed by the retailer.

In reality, we have limited intrabrand competition now. But because we have the possibility for intrabrand competition under existing law, the prices paid by retailers for beer and, thus, the price paid by consumers, is very competitive. Should one beer distributor of a particular brand get out of line with his prices, the retailer has the opportunity to buy the same brand from another wholesaler. This also helps maintain the lowest possible price.

The fact that competition between different brands may exist cannot override the fact that under exclusive sales territories there is no intrabrand competition. To use an example, suppose a consumer in Jefferson County, Ala., which is Birmingham, decides to buy a Chevrolet but only one exclusive Chevrolet dealer was allowed in that territory by the manufacturer. The customer would be able to buy the Chevrolet locally from only one dealer. Even though other makes of cars would be available, no doubt the lack of intrabrand competition from other Chevrolet dealers would mean a higher cost to the consumer. But the proponents of S. 1215 want to go one step further. Again using the Jefferson County Chevrolet buyer as an example, they want to prohibit anyone who lives in Jefferson County from going outside that county and buying a Chevrolet from anyone else.

These are the same circumstances Alabama retailers would face under legislation which was proposed in the Alabama Legislature, and that would be sanctioned by S. 1215. I think history shows conclusively that a monopoly, for whatever good it does, generally means the consumer ends up paying more.

There is already limited and diminishing competition in the beer business. The top six brewers in this Nation account for 83 percent of all domestic beer sales, and mergers are continuing to take place. In addition, extensive Alabama regulations already limit distribution of alcoholic beverages and the price that may be charged at the wholesale and retail level. We certainly do not need any more limitations on competition.

Perhaps a good example of how this bill would affect Alabama consumers and retailers can be drawn from the Indiana experience. You have already had testimony that says from a legislative study commission in Indiana there are reports that retail prices have dropped more than 20 percent since repeal of this law. This would happen because increased competition among wholesalers to go along with heavy competition at the retail level.

Business success in this country should be based on the individual company's ability to supply a product and service in a way and at a price that is acceptable to their customers, not through monopoly power. This is true of wholesaling as well as retailing, and it is as true for the beer industry as for anyone else. In a free market, everyone has an equal opportunity to excell and to fail. With this legislation, beer distributors are attempting to have the Federal Government insure that they cannot fail, with the insurance paid by higher prices to the consumer.

As I have stated, in Alabama we have successfully fought mandatory exclusive franchise legislation. We certainly are not the only State that so far has held off the beer barons. Enactment of this Federal legislation may very well make all of these efforts useless. First of all, beer distributors will use this legislation in the State legislatures and before alcoholic beverage control boards as an endorsement for exclusive territories and as an encouragement for the States to require such arrangements. In addition, beer distributors will use this law as a defense to efforts to get State mandatory exclusive territory laws and regulations repealed. But even more importantly, if this bill passes it will mean that States such as Alabama will be stuck with exclusive territories even if the State takes no action at all. That is because brewers and distributors see possible antitrust enforcement activity as the principal drawback to the use of exclusive territorial arrangements. If that possibility is eliminated, they will most likely switch to these arrangements in those States that do not already have them.

We believe that it should be the decision of the individual State to allow or require exclusive territories. If Alabama officials, exercising their rights under the 21st amendment, choose to adopt that distribution scheme in Alabama, then so be it. The Federal Government should not usurp that decision. S. 1215, by tinkering with the antitrust law, will have that effect.

As I mentioned in the beginning of my statement, the Alabama Legislature considered in the just concluded 1982 regular session a similar proposal to require exclusive sales territories for beer wholesalers. Because of intense opposition from many legislators, and from retailers, consumers, and the press, it was never considered on the floor of either body.

Perhaps my testimony can best be summed up by quoting briefly from two of the editorials that appeared in opposition to this bill in Alabama. Alabama's largest newspaper, the Birmingham News, said:

> The bill is an anticompetition, protectionist bill that would tend to place retailers at the mercy of big distributors and wholesalers, work against good service to retailers and against the best interests of consumers. In short, the bill would create state-sanctioned monopolies with all the ills accompanying monopolies.

The Birmingham Post-Herald said:

> The bill won't help consumers, retailers or those who would like to get into the wholesale business. If retailers want to sell the product, they will be forced to pay whatever the monopoly wholesaler decides and pass the cost on to their customers. There will be no shopping around.
>
> And if that's not enough reason to reject the proposal, it also opens the way to corruption. Limiting the number of firms or individuals who can become involved in any money-making enterprise is to make that enterprise or those who regulate it the target of unscrupulous individuals. Sooner or later, somebody will yield to the temptation.

The Alabama Retail Association believes that free enterprise and competition are what make this country great. We urge you to support free enterprise and competition by defeating this measure. Thank you, sir.

Senator SIMPSON. Thank you very much, Mr. Greer. I have several questions but because of the time problem, we have two more panels yet to hear from. I am interested in the issue of transshipping, which continues to come up from both sides of the issue.

I would ask Mr. Protos. You state that transshipping can best be controlled by self-regulation and self-policing within the industry. I would inquire as to what measures you might have in mind with regard to that.

Mr. PROTOS. At the present time you have State laws that would prohibit transshipping because of taxes. If you have transshipping across State lines, the only way you could do it is by paying the taxes into the State that you are shipping it to. If the taxes have already been paid, say, into the State of Maryland and you want to ship it to Pennsylvania, you have to have the taxes paid on it. So, in this area transshipping is illegal. Now, within a jurisdiction——

Senator SIMPSON. Yes, intrastate.

Mr. PROTOS. Intrastate. Well, one of the ways is just like one of the breweries putting their dates, the date on. Now, if you are transshipping bad beer, if all of it is openly dated to the public, you can see that the beer is old. And there are other means, I guess, in self-regulation that could control it.

Mr. MEIJER. Transshipping is just competition. It is simply whether or not you can ship from my county to your county or somewhere else. We need more competition, not less.

Senator SIMPSON. I think it would be interesting if you would share with the Congress the methods you might have in mind of self-regulation and self-policing with regard to that issue.

Mr. PROTOS. If you like, sir, we could submit it in written comment to you.

Senator SIMPSON. Thank you.

I was interested, too, in Mr. Greer in the reference—and I know what is given to us with regard to the study of the Indiana practice. Apparently the retail beer price has dropped more than 20 percent after the exclusive territorial agreements were banned.

Were there any other factors considered in that study which might have given rise to indication as to that drop in price?

Mr. **Greer**. We have some people from Indiana who will testify on that. From everything we have been able to see about it, this has been the result.

Senator **Simpson**. Thank you very much. I appreciate your being here.

The next panel consists of Frank J. Sellinger of the Joseph Schlitz Brewing Co. of Milwaukee; James Tito, vice president of Latrobe Brewing Co.; and Robert Pohl, general manager of the Hudepohl Brewing Co. of Cincinnati.

I hate to have to go to this grisly device here on the table, but I am going to go to that or else we will really have a hearing where you might be testifying to a senior staff member, and I do not like that. In fact, the Judiciary Committee has gone on record to speak very strongly against that. I am really even ready to scrub a bit of my next appointment. I am going to set this bomb here. You will have 7 minutes. It will come to 1 minute left on yellow, and then it goes off when it hits this here. I cannot tell you what happens, but those wires under your desk will give you some indication.

Please proceed, Mr. Sellinger.

STATEMENTS OF A PANEL CONSISTING OF FRANK J. SELLINGER, PRESIDENT, JOSEPH SCHLITZ BREWING CO.; JAMES L. TITO, VICE PRESIDENT, LATROBE BREWING CO.; AND ROBERT L. POHL, EXECUTIVE VICE PRESIDENT, HUDEPOHL BREWING CO.

Mr. **Sellinger**. My name is Frank Sellinger. On my left is Mr. Pohl, and on my right is Mr. Tito. We three have written statements which we desire to put into the testimony. In addition to that, I have two other documents, "the Brewing Industry Distribution System and the Case for Enactment of S. 1215, the Malt Beverage Interbrand Competition Act"; and "Malt Beverage Marketing in the Regulatory Framework, S. 1215, the Malt Beverage Interbrand Competition Act."

I would like to answer a few questions that were raised. First of all, Wisconsin does not have territorial rights. A wholesaler in Racine can bring beer into the city of Milwaukee even though the Schlitz Brewing Co. had its own distribution system there. So, that was one misstatement.

Mr. Meijer indicates no price competition, yet mentions the differential between different States.

I would also like to mention that profit is not a dirty word, in our mind. Wholesalers can only exist if they make a profit. Profit comes only as a result of sales in a very competitive marketplace. Beer profits are low at the brewery level, as indicated by industry profits. Brewery profits are among the lowest of any industry in the American marketplace. Beer profits are low at the wholesaler level, and that is indicated. Beer profits at the retail level cannot be exorbitant because beer has been on the low side on the consumer level. So, beer is not being overpriced to the consumer; otherwise, inflation would have caught up with it.

On another subject, territorial rights have been granted in 10 States. Seven States prohibit dual distributorships or implies existence of exclusive territories. Twenty-nine States either provide for sale territories or are silent on the subject. Four States allow dual distributorships in a specific geographic territory. There is only one State where exclusive territories are expressly prohibited.

In Indiana the big supermarkets are buying in big volume by buying from transshippers. They have discounted prices, which make it almost impossible for the little mom and pop stores to exist.

I would like to refer to my testimony of which you have a written copy. The résumé I have submitted indicates that I have been employed in the brewing industry for the past 46 years. I have had the good fortune to have held positions in brewing and packaging production and management of small, medium, and even two of the largest breweries today. Most of all, I have owned and operated a wholesale beer distribution system. On January 1, 1950, I opened the Hi-State Beverage Co., a beer wholesaling firm in Columbus, Ohio. I had been exposed to beer marketing at the Hudepohl Brewing Co. in Cincinnati and the Wagner Brewery, but I really desired to be a well-rounded brewery executive. The only way you can do that is to be exposed to beer wholesaling.

When I went into business, I not only invested virtually everything I had but borrowed extensively in order to start that business. That is the same thing that is true of many, many wholesalers today. Their entire livelihood is invested in their distribution. With the thousands of dollars invested in their operations, wholesalers need and deserve some sort of protection which this bill provides. It is not a guarantee, as the marketplace and interbrand competition is fierce. But it does help to stabilize the situation.

At the present time, in my old market, Columbus, Ohio, there are 10 wholesalers offering some 50 brands of beer to the retail accounts. The State of Ohio has an exclusive territory law. I wonder why the people from Michigan come over to Ohio and buy beer if the beer was so high in price, as has been asserted, because of an exclusive territorial law in Ohio.

I am familiar with the Ohio market and Columbus especially. I defy anybody to go there and tell me the consumer is being harmed by exclusive territories.

As I have stated previously, the interbrand competition there is extremely fierce. While one brand will dominate some sections of the city, in others another will. There is no national, regional, or even State market for beer. There are thousands of local individual markets, and this act will not be to the detriment of either the retailers or the consumers. Incidentally, Georgia, Michigan, New Hampshire, North Carolina, Tennessee, Vermont, and Oregon also provide exclusive territories and the competition within those States is as tough as anywhere in the country.

There have been many questions raised relative to the concern of American brewers in the act. Why is the brewer interested in this? We are interested because we need wholesalers who are profitable, who will be in business tomorrow, wholesalers who are in the community and hire a lot of people. Why, after all, should large and small brewers support legislation which benefits a separate segment of that industry, beer wholesaling? The answer is surprisingly simple. The three-tier system of distribution, established by the

FAA Act of 1935, creates an integral link between the brewer, wholesaler, and retailer. Thus, the brewer is dependent upon the beer wholesaler to deliver his malt beverage to the consuming public in a quality fashion, through all retailers, not specific retailers. This is central to our interest and support of S. 1215. Permit me to amplify.

The success and pride of any brewer is dependent upon the taste of our products and our wholesalers' sales efforts. Beer is a perishable food product. After packaging, its taste is adversely affected by extremes in temperature and age. Thus, after leaving a brewery, the manner in which our products are handled remains a primary concern.

Many brewers, including Schlitz, have specific agreements with their wholesalers outlining his, the wholesaler's, responsibility with respect to warehousing, delivery, distribution, and stock rotation. I must emphasize that, since the brewer does not really deal directly with the retailer, he is completely dependent upon the wholesaler as his primary contact with the outlet. The wholesaler, not the brewer, must assume both wide distribution to the many different types of outlets as well as proper handling and merchandising in those outlets. It is the wholesaler's efforts which result in the consumers having a choice of brands.

The wholesaler's lines of responsibility can only remain clearly drawn where one wholesaler is responsible for an appointed brand in an appointed area or territory. Failure to designate these geographic lines of responsibility causes the brewer to——

Senator SIMPSON. I am sorry, sir. I really am not a rude rascal, but we are not going to be able to finish if we do not limit the testimony. I emphasize to all of you and all of you who are going to testify that your written statement is part of the record. There is no reason to reread what is already part of the record. If you wish to summarize so that we can have an opportunity for questions, please do so.

Mr. SELLINGER. One word I would like to have is transshipment.

When the Schlitz Brewing Co. sold its plant in Syracuse and shipped the beer out of the city of Memphis, Tenn., it had to reduce its prices to the wholesalers in the northeastern part of the country. Those wholesalers having that reduced price could drop their beer in other areas because their price is low. Therefore, they can sell at a cheaper price than the wholesaler who is paying a higher price.

Transshipping puts the wholesaler at a disadvantage when he is trying to stay in his own territory.

Senator SIMPSON. Thank you. I must just ask you to conclude so that we may finish the testimony of other witnesses. I apologize for that but there is no other possible result. So, Mr. Tito, I must ask you to proceed please.

Mr. TITO. Mr. Chairman, my name is James L. Tito. I am vice president of the Latrobe Brewing Co., a small to midsized brewery. We make only Rolling Rock Premium Beer. We are located in southwestern Pennsylvania.

I am appearing here today in support of S. 1215. The Latrobe Brewing Co.'s view is a bit different than our larger brothers. We have a very small volume. We have far more at stake if the customer does not get the fresh quality product that we have built our reputation upon.

The brewing industry has been concentrated. The retail industry has been concentrated. The distributors are not. Because of this, the distributor is going to be the most effective force in promoting interbrand competition throughout the malt beverage industry. We look to this distributor-wholesaler as the individual who will be part and parcel with us for the survival of our brewery. His continual calling upon retailers is the only method by which we are going to compete with those who carry a large advertising budget. Success only follows repeated retailer calls by an effective wholesaler sales force.

Transshipping, on the other hand, carries our product only to the retailer's doorstep. It delivers. It does not sell. We feel that transshipping is something that will destroy our future. The movement of our product in volume into areas where we are either currently doing business or anticipate doing business is not the way by which we will survive.

A system of exclusive territories promotes accountability not only to the brewer but to the consumer. Since an authorized distributor would be responsible for selling our product in an assigned territory, he would be responsible for insuring the freshness and quality of this product. Without exclusive territories, the brewer, myself, is not able to guarantee that the beer that will be consumed will be at its best. As a result, both I, the brewer, and the consumer suffer.

We would note very firmly that exclusive territories would benefit small regional brewers much more so than they would national brewers. All brewers need distributors who will devote their energies to marketing the brewer's product agressively. Unless they can offer distributors an exclusive territory, these brewers with relatively small volume will have great difficulty attracting or retaining competent and agressive distributors who are willing to invest their time, their money, and their effort, all of which is necessary to make that brewer's brand a viable force in any marketplace. Thank you.

Senator SIMPSON. Thank you very much, sir. I appreciate your understanding of our time problem. Mr. Pohl, please.

Without objection, we will insert into the record your prepared statement, Mr. Tito.

Mr. POHL. Mr. Chairman, my name is Robert Pohl. I am executive vice president and general manager of the Hudepohl Brewing Co., a small-size brewery in Cincinnati, Ohio. I appear before you today to testify in support of S. 1215, the Malt Beverage Interbrand Competition Act.

In the testimony you have already heard this morning, the primary argument has focused on the need to preserve the three-tier system of distribution for malt beverages. As you know, the so-called small brewer is rapidly becoming an endangered species. The reasons for this are manifold. Of these, the single most threatening factor is the gradual disintegration of this three-tier system. Permit me to explain.

Transshipping, a practice which allows beer wholesalers to infringe upon the primary markets of other wholesalers, is at the heart of this threat.

A wholesaler who is willing to transship beer is generally only willing to transship national brands. The transshipper is practically guaranteed a sale when transshipping a nationally advertised brand of beer. The transshipper cannot and will not take a chance on transshipping brands produced by small brewers who can only effectively market beer in a limited geographical area.

In markets near the small brewer where the small brewer can compete on an even basis with the national brands, transshippers will come in from outside the market with national brands and sell them at a low price that undercuts the small brewer. Thus, our primary advantage for competing with the national brewers, lower prices, would be eliminated. The small brewer by his very nature must operate differently than the large national brewer. The small brewer relies on his own wholesale operation to help counteract the large advertising budgets of the national brewers. Small brewers cannot effectively compete dollar for dollar with the large national brewers, even in our home market. Thus, we rely on other factors such as excellent local service. It is our local wholesale operation that allows us to compete. We know our own wholesalers will care enough to give the retailer full service.

When transshipping wholesalers seek sales beyond their area of responsibility, the accounts sought tend to be the larger accounts, the accounts whose volume and service requirements are easy to accommodate and often more profitable. These sales obviously come at the expense of the wholesalers we appointed to be responsible for resale of our products in a particular marketing area.

As a result, our designated distributor may lose interest in the smaller accounts for which he is responsible and these retailers suffer. In order to be successful, our brands must be distributed in as many small retail outlets in our market as possible. With transshipping, only high volume retail accounts receive the wholesalers' attention.

Our brewery believes that a system of territorial exclusivity is the most efficient, if not the only, way we can continue to have our product available to the 90-plus percent of retail outlets in which we are presently represented, and thereby directly benefit the customers who patronize all of these retail outlets.

Finally, to the extent to which a manufacturer's distributor network inefficiently concentrates its efforts on the larger retailers, it fails to sustain the secure repeat business, fails to accord good services, and neglects smaller volume accounts. It is these small volume accounts which in aggregate sell a substantial volume of beer, and Hudepohl does not have the necessary resources to compensate for this.

The current system of distribution works. It allows the smaller brewer to compete effectively in a competitive marketplace. The current distribution system was established when there were no large national brewers. We need the system as it is in order to survive.

I urge you, please do not force the small brewer out of business. Thank you.

Senator SIMPSON. Thank you very much.

Without objection, we will insert the statement of Mr. Sellinger and the other material he prepared for us.

[The prepared statements of Messrs. Sellinger and Tito and additional submissions of Mr. Sellinger follow:]

Statement of Frank J. Sellinger

Joseph Schlitz Brewing Company

Mr. Chairman and Members of the Committee:

My name is Frank J. Sellinger and I am here today to speak in support of S. 1215, more commonly known as the "Malt Beverage Interbrand Competition Act."

A resume which I have submitted indicates that I have been employed in the brewing industry for the past 46 years. I have had the good fortune to have held positions in brewing and packaging production, in management of small, medium and even two of the largest breweries. I have also owned and operated a wholesale beer distribution business. On January 1, 1950, I opened the Hi-State Beverage Company, a beer wholesaling firm in Columbus, Ohio. I had been totally exposed to the marketing and sales groups at Hudepohl in the early 1940's and at the Wagner Brewing Company in the late 40's. I desired to have the well-rounded experience in beer wholesaling. I not only invested virtually everything I had been able to save but borrowed extensively in order to start this business. Thousands of other beer wholesalers put everything on the line for their business just as I did.

With the thousands of dollars invested in their operations, wholesalers need and deserve some sort of protection which this bill before you provides. It is not a guarantee as the marketplace and the interbrand competition is so fierce but it does help to stabilize the situation. At the present time my old market, Columbus has 10 wholesalers offering some 50 brands of beer to the retail accounts there and the State of Ohio has an exclusive territory law. I am familiar with that market and I defy anyone to go there and tell me the consumer is being harmed by exclusive territories.

As I previously stated, the interbrand competition there is extremely fierce and while one brand will dominate some sections of the city, in others another will. There is no national, regional or even state market for beer - there are thousands of local individual markets and this act will not be to the detriment of either the retailers or the consumers. Incidentally, Georgia, Michigan, New Hampshire, North Carolina, Tennessee, Vermont, and Oregon also have exclusive territories and the competition within those states is as tough as anywhere in the country.

There have been many questions raised relative to the concern of American brewers in an Act which, in their eyes, provides them no apparent advantage or gain. Why, afterall, should large and small brewers support legislation which benefits a separate segment of that industry - beer wholesaling.

The answer is surprisingly simple. The three-tier system of distribution, established by the Federal Alcohol Administration Act of 1935, creates an inextricable link between the brewer, wholesaler and retailer. Thus, the brewer is dependent upon the beer wholesaler to deliver his malt beverage to the consuming public in a quality fashion. This is central to our interest and support of S. 1215. Permit me to amplify.

The success and pride of any brewer is dependent upon the taste of our products and our wholesalers' sales efforts. Beer is a perishable food product. After packaging, its taste is adversely affected by extremes in temperature and age. Thus, after leaving a brewery, the manner in which our products are handled remains a primary concern. Malt brewers, including Schlitz, have specific written agreements with their wholesalers outlining his (the wholesaler's) responsibility with respect to warehousing, delivery and stock rotation of that brewer's products within the wholesaler's area of primary market responsibility. I must emphasize that since the brewer does not deal directly with the retailer, he is completely dependent upon the wholesaler as his primary contact with the outlet. The wholesaler, not the brewer, must assume both wide distribution to the many different types of outlets as well as proper handling and merchandising in those outlets. It is the wholesaler's efforts which result in the consumer's having a choice of brands.

The wholesaler's lines of responsibility can only remain clearly drawn where one wholesaler is responsible for an appointed brand in an appointed area or territory. Failure to designate these geographic lines of responsibility causes the brewer to lose an important measure of control over the quality of its products and control of distribution.

Needless to say, delivery of a fresh wholesome product is of vital importance to all brewers as is wholesaler sales efforts with retailers. This in large part, is why passage of S. 1215 is so critical.

When I was in the beer wholesaling business, as it is now, there are a great number of accounts which must be serviced in order to provide consumers with the greatest choice not only in brand availability but in outlet availability so that the consumer doesn't have to travel out of his immediate neighborhood to purchase the product. Many of these accounts are small "mom and pop" type stores while others, of course, are giant food chains. While the large supermarkets sell a great deal more beer, the livelihood of the small operator depends to a great degree on beer sales and as I noted before the consumer is served better as well.

In the absence of designated distribution territories, a practice known as "transshipping" has flourished. Under this practice, a wholesaler chooses to resell brand(s) outside the area of primary market responsibility. In many instances, wholesalers have distributed brands throughout entire states and even across state lines.

The ability of a transshipper to market beer outside the area of his primary market responsibility rarely if ever results from superior efficiency on the part of the transshipper. Rather, it is frequently due to lower F.O.B. prices for beer sent from the brewery to his territory and from the transshipper skimming the best accounts. You rarely see a transshipper servicing the small accounts I described before. He is dealing with large trailer loads of beer and this requires large single drops or certainly relatively few major retailers. A legitimate beer wholesaler really makes little or no profit on the small accounts but must service them anyway. If the large transshipper comes in and in effect takes the best accounts, the outcome for the legitimate wholesaler is predictable. Sooner or later he will go out of business.

"Drop-hauls" are often available to the transshipper, i.e., he may be able to transport the beer directly from the brewer to the retailer without it ever entering his territory. In such cases, the distributor is performing a mere paper transaction and can operate profitably with very small markups. In this way, he is able to win business from the distributor responsible for the marketing and maintenance of quality of the beer in the retailer's territory.

This widespread practice has a variety of detrimental effects. First, transshipping has serious economic consequences for the legitimate wholesaler and, as a result, increased unemployment as I noted before. There are numerous areas of the country where this situation has occurred. For example, because Rochester, New York represents a very strong market for competitive lowpriced local beer, it is necessary for shipping brewers to maintain lower prices for shipment of beer to wholesalers in that area than to other areas in Upstate New York.

As a result, distributors in the Rochester area are able to place orders for the shipment of beer to their facilities at the lower price, transport the beer into the higher priced markets, undersell the legitimate wholesalers there, and still maintain a comfortable profit margin. In some instances, the transshipper arranges that delivery be made directly from the brewer to his customer, and handles only the paperwork of the transaction. Under such circumstances the transshipper can more easily undercut the legitimate wholesalers in that area.

This, of course, has serious economic effects on the legitimate wholesaler. First, since he has less beer to sell because of the transshipper's encroachment, he may not enjoy previous economies of scale. The unit cost for the beer he handles is thus increased. This makes effective competition with the transshipper even more difficult. Moreover, as a result of his deteriorating position in the market, the wholesaler needs fewer drivers to deliver the product, and fewer employees generally. As a result of the transshipment patterns in New York State described above, many driver salesmen have lost their jobs, and many more will do so. This unfortunate set of circumstances exists in many other areas of the country, and is severe in states such as Massachusetts, Pennsylvania, Minnesota, and Indiana. When I was in Ohio we were familiar, of course, with the Indiana system. While the number of wholesalers has declined generally nationwide, the Indiana system has resulted in a loss of 38 wholesalers from 1972 to the present. This is a decline of about 19 percent. Nationally, the number of wholesalers has declined by 6 percent. Thus, increases in unit costs and deterioration of the legitimate wholesaler's competitive position have driven many wholesalers out of the business.

Another detrimental effect of transshipping is that there is no basic responsibility for the brewer's brands on a day to day basis in the marketplace. The transshipper will not necessarily follow through with the retailer as it may not be a permanent arrangement and since the local wholesaler has not sold the product, there is little obligation for him. Even if the transshipper has a "permanent" arrangement he does not have the continuous and constant attention in the marketplace so vital for success.

Transshipping also leaves the brewer less competitive in the marketplace. Everyone associated with our industry knows that the beer wars are won and lost in the streets where the firing lines are manned by our wholesalers. To remain competitive, wholesaler support is not necessary, but critical.

It is important to note that another advantage of the three-tier system in general, and exclusive territory laws in particular, is that they effectively isolate manufacturers from retailers, buttressing existing state prohibitions against tied houses, exclusive outlets and other anticompetitive, unfair trade practices, resulting in clear-cut channels of distribution. Because wholesalers are within state jurisdiction, they are more amenable to state control. Exclusive territory laws aid states in the enforcement of regulatory provisions, thereby helping to achieve the social ends of alcohol beverage control.

Furthermore, wholesalers are local, independent small businessmen who do much to support the communities in which they operate. For instance, a wholesaler owns land on which his warehouse sits and pays local property taxes. Most operating supplies are purchased locally. New warehouse or additions built on not only create more jobs but funds for those projects are borrowed from local banks. It stands to reason, of course, that these wholesalers are far less likely to make capital investments for these improvements if they are not assured of some protection.

In the final analysis, the consumer as well as the brewer and wholesaler needs protection from the numerous anticompetitive and inequitable effects of such a practice, as well as from the uncertain quality of transshipped products. The Malt Beverage Interbrand Competition Act is the best means to provide such protection.

Thank you.

Malt Beverage Marketing in the Regulatory Framework

S.1215

The Malt Beverage Interbrand Competition Act

June 21, 1982

United States Brewers Association, Inc.
1750 K Street, N. W.
Washington, D. C.
20006

MALT BEVERAGE MARKETING IN THE REGULATORY FRAMEWORK

In other parts of this report we have described the basic economic aspects of the brewing production/distribution system; the scope and magnitude of the wholesale and retail distribution system and the concentration over time within the entire brewing and retailing segments specifically.

In this particular section we will consider the marketing of malt beverages in the United States with emphasis on the impact of the regulatory framework, the differences between beer and other products, and how beer marketing has evolved. Lastly, we will consider the chief problem in beer marketing -- transshipping, the form of "free riding" to which the provisions of S. 1215 are directed and intended to prevent.

The Regulatory Framework

The three tier system of production and distribution of malt beverages in the United States is not the choice of the brewer, the wholesaler, or the retailer. It is the product of regulation which also is directed from three levels -- Federal regulation (the Federal Alcohol Administration Act and the Federal excise tax of $9 per barrel), state regulation under state statutes and by virtue of state excise taxes, and under local option statutes permitted by state law and through differentials in sales taxes imposed upon malt beverages.

No one may produce a malt beverage, wholesale a malt beverage, or retail a malt beverage without being licensed. In order to produce a wholesale malt beverage, a brewer and a wholesaler must qualify under the FAA Act and pay an occupational tax. In order to retail a malt beverage, a retailer must obtain a state and in addition, if required by local option laws, a local license to retail the product.

Unlike other products in commerce, alcoholic beverages, including malt beverages, are the creature of public policy and are rigidly regulated at every step in production and distribution. Under the Twenty-First Amendment, the states are granted plenary powers to prohibit entirely the sale of malt beverages or to rigidly describe the methods by which they will be distributed or sold.

There is no uniformity beyond the FAA Act. There is no uniformity in the various state and local laws and regulations governing the distribution and retail sale of malt beverages. The basic selling tools available to all other marketers of products, such as price promotions, discounts, multi-brand marketing, and advertising are in the case of the brewers, wholesalers and retailers of malt beverages restricted to the point where it can be said that a free market for malt beverages does not exist. State laws without fail proscribe the use of these tools and, additionally, exact high excise taxes and sales taxes to discourage and regulate consumption of the product. Further, the differences in state laws and regulations are vast. Accordingly, the marketing of malt beverages is different from other products which reach the consumers through retail outlets throughout the country.

History Since Repeal

When Prohibition was repealed in 1933, after 13 crime-ridden years, not only did the Federal and state governments tighten controls, but the brewers, distillers and vintners adopted policies of self-regulation as well. The industry, recognizing the need for such a system, was fully prepared to cooperate. Experience and the individual needs of each state, with oversight by the Federal Government,has given us a strict but irreconcilable system from state to state.

The Federal Alcohol Administration Act (FAA) was put into place soon after Prohibition. Although recent changes have greatly changed the Bureau of Alcohol, Tobacco and Firearms, BATF is still responsible for the administration and enforcement of the Act. These responsibilities include the administration of regulations specifying who may qualify as a brewer and the collection of both brewer and wholesaler occupational taxes, the regulation of trade practices, advertising and labeling. (Most states have, in addition to their own statutes and rules, adopted various versions of the FAA Act. Federal/state enforcement cooperation fluctuates depending on outside factors.)

Under the FAA Act, the Federal Government must approve all alcoholic beverage advertising. This approval is sufficient for most states, but some insist on putting their own stamp on those ads as well. Therefore, advertisers must also submit to numerous state agencies even if BATF has already approved the advertisement.

This leads us to the next tier of the multi-level scrutiny to which the brewing industry is subjected. The different regulatory structures of each state tend to limit changes to fit the particular state system with its own peculiarities of its population, geography (urban v. rural), dry sentiment and general drinking habits. The most dramatic difference lies between the control (monopoly) versus the open (license) methods. Thirty-two states plus the District of Columbia are "open," i.e., the states license retailers and wholesalers to handle the distribution and sale of alcoholic beverages. The other 18 states are "control" -- the states themselves actively engage in the buying and selling of liquor at wholesale and nearly all also engage in retail sales.

Most state regulations are promulgated by an independent state agency, the majority of which are headed by a single person. These agencies are also responsible for administration, licensing and enforcement of state laws as set by the state legislature, and for the collection of revenues as well. In addition, the legislatures of the various states have provided their Alcoholic Beverage Control (ABC) agencies with rule-making power for specific situations. Licensing further serves as a device to restrict participation in the industry to those deemed qualified. As a license confers only a privilege, not a vested interest, it can be tailored for particular needs, yet this adds still another layer of complexity to the system as a whole.

In the official study by the Joint Committee of the States to Study Alcoholic Beverage Laws, published in 1973, the Committee came to the conclusion, as it had twice previously, that it would be virtually impossible to recommend any uniformity or standardization of ABC laws, regulations or operations. This conclusion is easily borne out by the innumerable differences between the advertising laws and regulations of the states. A few issues facing each state with regard to advertising are: billboards, circulars, consumer and retailer novelties, product displays on retail premises, whether the FAA regulations have been adopted, newspaper and magazine advertising, radio and T.V., the use of premiums or other inducements, samples and signs. For example, in several states, such as Vermont, Utah and Oklahoma, billboard advertising of alcoholic beverages is flatly prohibited, but many other states have no restrictions whatsoever.

Finally, but not least importantly, after Prohibition was lifted, 32 states provided that their citizens had local option, i.e., could vote for or against the sale of liquor in various cities or counties of the states. Local authorities in certain jurisdictions are also empowered to impose sales taxes in addition to the state excise taxes and other restrictions, including those on advertising and hours of sale.

It is obvious from these several tiers of restrictions -- Federal, state and local -- that the brewing industry is particularly guarded as to its advertising and marketing procedures. It is not an industry like any other in this respect, and deserves special consideration.

Thus, it is clear that brewers, wholesalers and retailers are dealing with a far different set of rules in producing and moving the product to the consumer than are most other manufacturers. The other alcoholic beverage products, distilled spirits and wine, clearly have the same general type of legal restrictions.

In view of these constraints, what have been the adjustments made by the brewing/distribution system in order to cope with such restrictions.

The answers to this are based not only on the evolvement of laws over time, but changes in the social and cultural aspects of the states and the country. While it is not the purpose of this document to describe in detail how beer marketing has developed, a short overview may be in order.

After Prohibition, malt beverages were produced in some 750 different locations throughout the country and were distributed to wholesalers and then retailers in an extremely limited geographic region by today's standards. Beer is a relatively expensive product to transport considering its value and any brewer wishing to expand his area of sales would have to consider the freight differences when shipping to another market.

Thus, for many years after the repeal of Prohibition, this country had a number of areas which might be called "brewing centers." That is, there were a large number of areas within which were located one or more local or regional brewers.

The local or regional brewers, for competitive reasons, priced their beers at levels which would permit their wholesalers to generate the lowest consumer prices possible within their geographical areas of operation. Any brewer desiring to sell in that area would have to consider these varying regional prices when making their decisions to ship into those areas, and in pricing their products. While there are fewer brewers today, the basic local pricing situation still exists.

Beer is priced for sale to wholesalers by the case. There are 24 12-ounce cans or bottles in a case. The number of containers of other sizes in a case varies with the sizes of the containers. Within a case, beer is packaged by the brewer or importer in various sorts of cartons for retail sale, e.g., six-packs, eight-packs, ten-packs, twelve-packs, and others. Some cases are packed loose, principally for sale to taverns and restaurants, where beer is dispensed to the customer a bottle or a can at a time. Every brewer or importer markets its brand or brands of beer in several such cartons but not all of them in all markets at all times. Domestic brewers generally sell beer to wholesalers f.o.b. the brewery. Importers generally sell beer to wholesalers c.i.f. port of entry (sometimes designated f.o.b. port of entry), although some importers also maintain warehouses from which they sell f.o.b.

The many brands of beer fall into approximately five price categories. From least to most costly these are: (1) "price" or "generic" beers (chain-grocery house brands, for example); (2) "popular" or "regional" priced beers; (3) "national" or "premium" priced beers; (4) "super-premium" beers; and (5) imported beers. A single brand of beer is sometimes competitively marketed in one price category in one local market and, at the same time, in another price category in a second local market. From time to time, brewers and importers engage in the test marketing of new brands or new packages of existing brands within specific local markets in an area.

In the 1930's, the chief means of selling beer was in draught form and in refillable bottles. Both these packages were expensive to ship and return and as a result, the need for less costly containers arose. The first answer to the shipping problem came with the development of the beer can in 1935 and while World War II delayed its widespread use domestically, it was used extensively by the Armed Forces and after the war, sales in that container started to boom. The can and the glass companies' competitive response to it, the one-way bottle, enables brewers to ship relatively more cheaply and expand their markets accordingly.

The shipping breweries which had penetrated new markets in 1946 with minimal quantities of beer now had the product and the light-weight, one-way containers available to ship to these distant markets. Local breweries which had withdrawn from markets to protect more profitable local markets found it difficult to re-enter those markets which they had left without product the year before. In addition, many local breweries did not have the equipment to fill flat top cans. So, for the first time, the shipping brewery had certain advantages not formerly available to them.

In today's marketplace, a brewer or importer wishing to expand his region of sales normally must locate a wholesaler in the area in which he desires to sell and reach an agreement with that wholesaler on how his product will be distributed. That agreement, of course, is subject to the laws of the state.

Brewer Marketing Agreements

Most distributorship agreements, in general, contain many of the same provisions, although the wording and order of presentation may vary.

However, certain matters of importance to a particular brewer may also be contained in the distributorship agreement.

In general, provisions dealing with the following matters will appear in distributorship agreements:

1. Agreement by the distributor (wholesaler) to use his best efforts to promote, develop and sell the brewer's product, including satisfactory warehousing, and in the case of some brewers, provision for refrigeration of warehousing;

2. Terms of payment or extension of credit, as permitted by state law, for payment of the brewer's product.

3. Assignment or designation of primary market or territory. These can be exclusive or nonexclusive, dependent on both the brewer's desire and the requirements of the applicable state law;

4. Reserved rights of the brewer with regard to new products, or the discontinuance of presently marketed products;

5. Advertising responsibilities of the wholesaler;

6. Adherence to, and observance of, federal, state and local laws and regulations;

7. Obligation of the wholesaler to obtain state or local licensing, and payment thereof, as well as payment of applicable taxes.

8. Responsibility of wholesaler to abide by the policies, sales and marketing practices, and methods of the brewer;

9. Use of the brewery name, insignia, and other brewery trademarks;

10. Written approval of the brewer upon the proposed sale or transfer of a distributorship; and

11. Termination.

With regard to termination, it is necessary to discuss the various types in more detail.

a. A wholesaler upon written notice to the brewer, usually thirty days, may terminate his agreement for any reason.

b. A brewer may wish to terminate for deficiency in performance of the wholesaler, either based on sales performance, or the standards and methods of merchandising used by the wholesaler. The distributorship agreement generally outlines the following remedies in the case of this type of termination:

(1) Written notice to wholesaler;

(2) Right of appeal to regional marketing manager, with further appeal to the responsible officer at the brewery level;

(3) Arbitration;

(4) Period for correction of deficiencies;

(5) Payment for liquidation, usually in an amount equal to the net earnings before taxes within the last fiscal year or annual accounting period of the wholesaler;

(6) Repurchase or credit for the brewer's stock (product);

(7) Return of all brewer point-of-sale materials and cooperage; and

(8) In some cases, fair market value purchase of certain tangible assets, such as delivery vehicles.

c. Upon a written notice, usually with a short period of time, immediate termination for cause by a brewer will be effectuated for the following reasons:

(1) Assignment for the benefit of creditors;

(2) Receivership or insolvency of the wholesaler;

(3) Bankruptcy, or the filing of a petition thereof;

(4) Violation of Federal and state law;

(5) Conviction for a felony;

(6) Revocation, suspension, or failure to renew a Federal basic permit or local or state license;

(7) Fraudulent conduct or dishonesty; and

(8) Failure to pay for purchases from the brewer in accordance with brewer's established terms of sale.

In the case of immediate termination, the brewer will repurchase the wholesaler inventory of the brewery's product as of the date of termination, usually the laid-in cost of such inventory. In addition, the wholesaler is required to return all brewer point-of-sale materials and cooperage.

As this system evolves, wholesalers naturally handle many brands of beer made by different brewers. While the reasons for brand segmentation in terms of consumer's options (light beers, premiums, populars, etc.) are a subject of a less critical nature to this paper, suffice to say that brewers have responded to consumer demand by offering many types of beer (ale, light, etc.), package sizes, container types and units (six-pack, twelve-pack, etc.).

While normally a wholesaler may not handle "directly competing" brands (*e.g.*, two national premiums), in some instances he might and he certainly will carry many types and styles of domestic beer and imports. There are very few wholesalers who would handle only one brewer's products.

Transshipping, The "Free Riding" of the Brewing Industry

Transshipping is intra-brand competition, not inter-brand competition. It occurs where a wholesaler leaves his territory to sell to a volume purchaser in the territory of another wholesaler of a same brand.

The ability of a transshiper to market beer outside the area of his primary market responsibility rarely, if ever, results from a superior efficiency on the part of the transshipper. Rather, it is frequently due to lower f.o.b. prices for beer sent from the brewery to his territory. In addition, "drop-hauls" are often available to the transshipper, *i.e.*, he may be able to transport the beer directly from the brewer to the retailer without it ever entering his territory. In such cases, the distributor is performing a mere paper transaction and can operate profitably with very small markups. In this way, he is able to win business from the distributor responsible for the marketing and maintenance of quality of the beer in the retailer's territory.

This widespread practice has a variety of detrimental effects. First, transshipping has serious economic consequences for the legitimate wholesaler and, as a result, increases unemployment. There are numerous areas of the country where this situation has occurred. For example, because Rochester, New York, represents a very strong market for competitive low-priced local beer, it is necessary for shipping brewers to maintain lower prices for shipment of beer to wholesalers in that area than for shipment to other areas in upstate New York.

As a result, distributors in the Rochester area are able to arrange for the shipment of beer to their facilities at the lower price, transport the beer into the higher-priced markets, undersell the legitimate wholesalers there, and still maintain a comfortable profit margin. In some instances, the transshipper may arrange that delivery will be from the brewer to his customer, and handle only the paperwork of the transaction. Under such circumstances, the transshipper can even more easily undercut the legitimate wholesalers in that area.

This has serious economic effects on the legitimate wholesaler. First, since he has less beer to sell because of the transshipper's encroachment, he may not enjoy previous economics of scale. The unit cost for the beer he handles is thus increased. This makes effective competition with the transshipper even more difficult. Moreover, as a result of his deteriorating position in the market, the wholesaler needs fewer drivers to deliver the product, and fewer employees generally. As a result of the transshipment patterns in New York State described above, many have lost their jobs, and many more will do so. This unfortunate set of circumstances exists in many other areas of the country, and is severe in states such as Indiana, Massachusetts, Pennsylvania, and Minnesota.

Indeed, increases in unit costs and deterioration of the legitimate wholesaler's competitive position may be so severe as to drive many wholesalers out of the business. In such cases, effects on employment are even more extreme. In addition, the loss of these wholesalers often leads to statewide distribution systems, and results in increased concentration at the one level of the malt beverage distribution industry responsible for effective interbrand competition.

The number of licensed retail outlets in any geographic territory assigned to any wholesaler is always limited. The wholesaler's agreement with the brewer requires him to service all licensed retailers in his territory. Indeed, in most instances state law also imposes that requirement upon the wholesaler.

The volume of beer sold to each of these licensed retail outlets will vary widely. The wholesaler must spread his costs over the sales to all of the licensed retailers. If he is deprived of his ability to sell to the higher-volume, licensed retail outlets due to transshipments, his territory is being skimmed and he has lost his most profitable accounts. If he is to stay in business, he must, of course, raise the cost to the remaining licensed retail accounts available to him, go out of business, or become a transshipper himself. In the latter event, the brand with respect to which the transshipping is occurring now becomes the victim of a chaotic distribution system, and everybody associated with that brand, including the consumers thereof, suffer. Large licensed retailers, principally grocery chains, have been tempted to and have seduced wholesalers to become parties to transshipping on the basis of their high volume of retail sales. Even if it can be assumed, and it cannot be, that these large volume retailers who have encouraged transshipment pass through their cost saving to the ultimate consumer of the brand, it cannot be demonstrated that the consuming public as a whole has been well served in that geographic area, since only those consumers who purchase from the chain store or other volume purchaser engaging in transshipping will receive the benefit if it is passed through. All of the rest of the consumers who purchase from the remaining licensed retailers must, of necessity, pay a higher price with respect to that brand.

Transshipping also leaves the brewer less competitive in the marketplace. Everyone associated with our industry knows that the beer wars are won and lost in the streets where the firing lines are manned by our wholesalers. To remain competitive, wholesaler support is not necessary, but critical.

The solution to this multitude of problems is the establishment of exclusive territories for beer wholesalers. The consumer as well as the malt beverage brewer and wholesaler needs protection from the numerous anticompetitive and inequitable effects of transshipping. The Malt Beverage Interbrand Competition Act is the best means to provide such protection.

THE ADVERSE REPORTS OF THE DEPARTMENT OF JUSTICE AND THE FEDERAL TRADE COMMISSION

In departmental reports addressed to this Committee on April 13 and June 11, 1982, respectively, the Department of Justice and the Federal Trade Commission opposed the enactment of S. 1215. Neither of these reports attempted to address the special problems of the malt beverage industry and its distribution system. Only cursory attention is given to the impact of the Federal and state regulatory systems upon the distribution of malt beverages. Indeed, both reports assume that the marketing of malt beverages is like the marketing of other consumer products and that a free market exists for the manufacture, distribution and sale of malt beverages.

Both reports concede that the rule of reason contained in Continental TV, Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977), is designed to and would protect exclusive territorial agreements between brewers and wholesalers of malt beverages from "free riding," that is to say transshipping.

The gravamen of both reports appears to be (1) a general objection to any exceptions to the Antitrust Laws of the United States, however warranted, and (2) to the premise that exclusive territorial arrangements between brewers and wholesalers might tend towards collusion amongst wholesalers who are in "inter" as distinguished from "intra" brand competition, because of "concentration" in the wholesale distribution of malt beverages; and, further, that brewers might encourage such collusion in order to share in any profits resulting from such collusion.

Both the Justice Department and the FTC can be forgiven for their ignorance of, and their lack of research into, the specific Federal and state statutes and regulations thereunder which deny the benefits of a free market to the malt beverage industry. However, neither the Department or the Commission can be forgiven for their lack of economic analysis, given their assumptions of a free market. As pointed out above, the rate of profit of both brewers and wholesalers is modest with respect to other manufacturers and distributors of consumer products. As is also pointed out above, the cost of malt beverages to consumers ranges far below that of other beverages consumed in the country. What has not been pointed out above is this. Without independent wholesalers who are protected from "free riding" and intra-brand transshipping, regional and small brewers will have no way of getting their products to market. It is doubtful if any brewer of malt beverages in the United States could afford an independent distribution system, even if the law permitted it and it does not. Assuming that it could be done at all, only two brewers could conceivably marshal the capital required to do so. The rest of the brewers would be left without a distribution system. The point is this. Without the independent wholesaler, protected by a geographic agreement that grants him the exclusive right to sell within that territory, concentration at the brewer level will increase. To the extent that concentration increases at the brewer level, it must, of necessity, cause concentration at the wholesale level since there will be fewer brewers to serve, if, indeed, any wholesalers survive at all. Thus, denying the protection of S. 1215 to the brewing industry and its distribution system will cause in and of itself the result which both the Department and the FTC profess to fear.

Greater concentration alone will not be the only result of denying enactment of S. 1215. Public policy will suffer. The states and their localities will have no one to look to for the collection of their excise taxes. There will be no wholesaler to deal with local deposit laws. State liquor administrators will have no independent wholesalers to aid in the enforcement of state and local law respecting illicit sales by unlicensed retail outlets. Consumers, however, will lose the most. The record of low consumer prices and low industry profits will be affected because, as the number of brewers decreases and the number of wholesalers decreases, costs will inevitably go up together with consumer prices.

During the course of the hearing on S. 1215, we know that the members of the Judiciary Committee will desire the Justice Department and the Federal Trade Commission to address the facts and special circumstances concerning the brewing industry and its distribution system as related in this paper, and to ask the Department and the Commission to reexamine their positions in the light of the special circumstances surrounding the industry. It is the hope that this Committee will speedily report S. 1215 to the Senate of the United States and secure its prompt passage by the Senate.

The
Brewing Industry Distribution System and the Case for Enactment of S.1215 The Malt Beverage Interbrand Competition Act

June 21, 1982

United States Brewers Association, Inc.
1750 K Street, N. W.
Washington, D. C.
20006

AN ECONOMIC PROFILE OF THE MALT BEVERAGE PRODUCTION AND DISTRIBUTION SYSTEM IN THE UNITED STATES

The Brewing Industry and Consumers of Beer

The nation's 43 brewing companies currently have 80 plants throughout the United States. The sales of domestic brewers in the United States represent approximately 97 percent of all beer consumed in this country, and about 90 percent of the beer distributed in the United States is sold through independent beer wholesalers. The remainder is sold through brewer branch operations.

In 1981, the total value of beer sold by brewers and importers was approximately $11.0 billion which does not include excise taxes (federal and state) which amounted to close to $2.7 billion. Consumers spend approximately $31.4 billion for malt beverages of all kinds (domestic and foreign) in both on-premise (taverns, restaurants, hotels, etc.) and off-premise (supermarkets, convenience stores, package stores, etc.).

Beer is consumed by approximately half of the adult population and close to 50 percent is purchased by those with incomes of $20,000 or less (Table 1). As Table I reveals, those households with income of less than $20,000, consumed approximately 47 percent of all beer, yet accounted for only 31 percent of the nation's income but, at the same time, represented 60 percent of all households. Clearly beer is the working man's drink, and is the fourth most popular beverage in the country behind soft drinks, milk and coffee. More than two-thirds of all men drink beer and almost 40 percent of all women.

The brewers' products are among the most highly taxed in the nation; about 13 percent of the consumers' dollar represents excise and sales taxes on malt beverages. This compares with about five percent for most products purchased today.

Table 1

Distribution of Beer Consumption and Family Personal Income by Income Groups

Income Bracket	Percent of Total Consumption	Percent of Total Income	Percent of Households
Under 8,000	10.7	5.7	23.2
8,000-14,000	14.7	10.5	19.5
14,000-20,000	21.7	14.4	16.9
20,000-25,000	17.6	14.1	12.4
25,000 & Over	35.3	55.3	28.0
	100.0	100.0	100.0

Source: Consumption - National Family Opinion, Inc., 1980 "SIP" Study.
Income & Households, 1979. United States Department of Commerce.

When one speaks of the "brewing industry," one does not simply refer to breweries and brewery workers. For in addition, there are the farmers who grow the agricultural products (barley, corn, rice, hops, etc.) used in brewing. There are also the suppliers of cans, paper board boxes, bottles and adhesives. Ther are approximately 4,500 beer wholesalers and their employees. Finally, there is the transportation system which insures that the malt beverages enjoyed by American consumers are fresh and wholesome.

Here are several examples to provide a general idea of the scope of these contributions on an annual basis:

- There are currently 80 brewing plants operating in some 29 states which employ close to 47,000 persons with an aggregate payroll in excess of $1.5 billion. They have gross assets of over $5 billion and beer sales in 1981 in excess of $10.4 billion.
- The 4,500 licensed wholesalers employ approximately 80,000 workers with a total payroll of $1.4 billion. These small businessmen are the backbone of many smaller communities.

- In 1980, the brewing industry purchased $1.1 billion in agricultural products. These included: hops from the Pacific Northwest; barley, corn, and wheat from the Midwest; and rice from the South and Southwest, as well as the West Coast.
- In 1980, the brewing industry paid more than $4.2 billion for packaging materials. Many of the bottle and can plants are located in a region especially hard hit by the ravages of inflation and unemployment, the Northeast and Midwest. The can and bottle manufacturing employees dependant upon the beer industry number over 30,000.
- More than $500 million was invested in the transportation industry for shipping both raw materials and packaged beer.

In addition, there are the approximately 500,000 retail outlets which bring the finished products to the consumer. These establishments, which rely heavily on the sales of malt beverages, employ literally millions of workers.

Rate of Profitability of Brewers

The brewing industry's rate of profitability is lower than that of total U.S. industry. Looking solely at brewers, without including their distributors, net income after taxes in 1980 stood at 4.3 percent of sales while the profitability rate for American industry as a whole was 4.9 percent (according to figures compiled by Citibank of North America). Ten years previously, however, brewing industry profitability was higher than that of U.S. industry in general, with the brewing industry earning 5.7 percent of net sales, while the total American industry average was 4.5 percent. Thus, brewing industry profitability as a percent of sales decreased both absolutely and relatively during the decade of the '70's.

The Distribution System

Beer is distributed to consumers through what is termed the three-tier system: brewer--beer wholesaler--retailer.

Other sections of this testimony detail the reason and history of the development of the three-tier system for alcohol beverages and beer. The following table reveals the quantitative changes over time in the three-tier system, namely the number of brewers, wholesalers and retailers.

Number of Breweries, Wholesalers & Retailers
1948-1979

	Breweries	Merchant Wholesalers	Eating & Drinking	Retail Liquor Stores	Food Stores
1948	466	5,668	346,556	33,422	504,439
1954	310	5,791	319,657	31,240	384,616
1958	252	5,879	344,740	37,068	355,508
1963	211	5,694	334,481	40,188	319,433
1972	139	5,038	359,524	41,491	267,352
1977	94	4,795	368,066	44,354	251,971
1979	90	4,539	N/A*	N/A	N/A

*N/A - Not Available.

Source: U.S. DEPARTMENT OF TREASURY, BUREAU OF ALCOHOL, TOBACCO & FIREARMS, CENSUS OF WHOLESALE & RETAIL TRADE, COUNTY BUSINESS PATTERNS, U.S. DEPARTMENT OF COMMERCE.

The above table demonstrates the decline in numbers of the entire distribution system for beer which occured, incidentally, even as the population increased. And, while the retail outlets do not necessarily represent outlets which are all licensed to sell beer (state and local laws prevail), they do represent an overview of main potential outlets throughout the country. The total figure for retail outlets in 1948, 884,417 compares with 664,391 for 1977. While these data provide overall trends, let us consider more specifically the concentration of the three-tier system and the competitive forces involved.

The beer wholesaler, while declining in numbers, has remained the basic link between brewer and retailer. And, in the cases of both the brewer and the retailer, we have seen increasing concentration even within the past five years.

In 1975, the top five brewers produced 66 percent of total beer sold in this country; by 1981, that figure was almost 75 percent. The recent activity among brewers with respect to mergers, acquisitions, etc., indicates that this trend will continue.

The Wholesaler

The table below provides the most current information available relative to the nation's beer wholesalers and the size of their operations with regard to employment. This information was compiled by the United States Department of Commerce and clearly demonstrates that beer wholesalers are basically small businessmen. During this difficult period for our nation's economy when small business failures, in particular, are so common and are occuring at increasing rates, the Malt Beverage Interbrand Competition Act could stabilize the economic situation in the brewing industry without lessening competition.

The table below reveals that in 1979, a little over one-fourth of the nation's beer wholesalers had from one to four employees. Similarly, almost three-fourths of the country's beer wholesalers had less than 20 employees. Over 60 percent of the workers in the beer wholesaling distribution system came from firms with less than 50 employees, and these firms represented nearly 95 percent of all beer wholesalers in the country. Clearly, this is basically a small business when measured in terms of employment distribution.

1979 Number of Beer Wholesalers by Employment and Size

Size	Number of Merchant Wholesalers	Number of Employees
1 - 4	1,172	"D"
5 - 9	1,017	7,405
10 - 19	1,187	16,796
20 - 49	846	25,594
50 - 99	246	16,970
100 - 249	70	9,860
250 - 499	1	"D"
500 - 999	--	--
TOTAL	4,539	80,401

Source: COUNTY BUSINESS PATTERNS, U.S. DEPARTMENT OF COMMERCE

Table 2 on Page 7 reveals the number of wholesalers, employees and payroll for each state.

Turning to sales, the 1980 total for the 4,714 U.S. beer wholesalers was $17,302,500,000. According to the Beverage Data Bank of the Beverage Marketing Corporation, approximately 3,935 wholesalers, or about 84 percent, had annual sales of $5 million or less. Additionally, those with sales under $5 million accounted for almost 45 percent of the total sales of malt beverage wholesalers. The 466 wholesalers with sales between $5 million and $10 million accounted for $3.5 billion, or 20 percent of total sales. Clearly, this industry is not dominated by a few, and a review of the regional and state concentration data supports a similar conclusion. Beyond the concentration aspect is a concern that three to four relatively large wholesalers could dominate a specific market. But it must be emphasized, that they would be competing with each other with different brands which clearly would not be to the detriment of the consumer. Thus, the outlook for the brewing industry is that it will remain among the most intensely competitive in the country.

The Wholesaler's Rate of Profitability

According to a National Beer Wholesalers Association survey of some 200 wholesalers with sales of $1.4 billion located in 42 states, cost of goods sold are some 78 percent of net sales. This survey, prepared by the School of Business Administration of St. Louis University, shows gross profit for all firms to be approximately 22 percent, net operating expense at 17.7 percent of net sales and net operating profit before income taxes at 4.63. Selling expense is 4.2 percent of net sales, warehouse 7.4, administrative 5.3 and other 0.8 percent.

The Wholesaler as Tax Collector

Individual state governments benefit from the three-tier system. By collecting from local wholesalers as opposed to non-resident suppliers or from thousands of retailers, the state's task is greatly simplified. This method enables the state

TABLE 2
1979 NUMBER OF BEER WHOLESALE ESTABLISHMENTS, PAYROLL & EMPLOYEES BY STATE

STATE	MERCHANT WHOLESALER ESTABLISHMENTS	PAYROLL (000)	EMPLOYEES
ALABAMA	56	$ 22,100	1,250
ALASKA	4	1,010	100
ARIZONA	42	14,404	897
ARKANSAS	54	8,315	480
CALIFORNIA	255	121,796	6,879
COLORADO	54	18,136	1,086
CONNECTICUT	23	14,468	789
DELAWARE	6	4,689	226
DIST. OF COLUMBIA	7	4.433	247
FLORIDA	97	51,026	2,863
GEORGIA	69	26,452	1,784
HAWAII	12	2,229	159
IDAHO	43	7,360	479
ILLINOIS	202	84,500	4,103
INDIANA	169	35,598	2,238
IOWA	102	18,400	1,030
KANSAS	57	12,611	689
KENTUCKY	77	21,300	1,350
LOUISIANA	60	24,564	1,679
MAINE	25	10,424	640
MARYLAND	67	23,729	1,293
MASSACHUSETTS	35	30,525	1,570
MICHIGAN	187	89,750	4,174
MINNESOTA	131	23,965	1,403
MISSISSIPPI	51	11,952	804
MISSOURI	127	35,742	2,240
MONTANA	45	8,033	515
NEBRASKA	56	9,311	535
NEVADA	14	3,877	242
NEW HAMPSHIRE	18	5,084	310
NEW JERSEY	50	37,100	1,910
NEW MEXICO	26	5,028	347
NEW YORK	305	95,317	6,174
NORTH CAROLINA	96	30,753	1,951
NORTH DAKOTA	21	3,481	214
OHIO	143	75,444	4,470
OKLAHOMA	55	13,339	861
OREGON	96	20,434	1,124
PENNSYLVANIA	598	57,609	4,618
RHODE ISLAND	5	5,746	306
SOUTH CAROLINA	60	17,723	1,101
SOUTH DAKOTA	31	4,800	400
TENNESSEE	62	26,358	1,668
TEXAS	356	91,900	5,700
UTAH	20	5,338	340
VERMONT	13	10,260	490
VIRGINIA	85	32,031	2,001
WASHINGTON	114	34,823	1,775
WEST VIRGINIA	63	9,842	601
WISCONSIN	168	34,425	2,086
WYOMING	27	3,444	210
	4,539	1,360,978	80,401

SOURCE: COUNTY BUSINESS PATTERNS, U.S. DEPARTMENT OF COMMERCE & USBA ESTIMATES.

to ascertain the source, authenticity and date of shipments into the state as well. The system works so well that many states have eliminated tax stamps and rely solely on the reporting (or accounting) method of the wholesaler. Taxes collected are then either deposited entirely into a state's General Revenue Fund, partially reserved for important programs, or funneled back into use by the municipalities. These tax revenues form a major part of each state's budget plan every year.

Table 3 shows the estimated dollar value of wholesale beer sales along with taxes paid by the brewing industry to the Federal government and to state and local jurisdictions in 1980. These tax contributions are in addition to the "normal" (income, property, etc.) taxes paid by all businesses.

The Retailer

Let us now consider the third tier of the malt beverage production/distribution system--the retailer. While there is a lack of "hard" data available concerning the sale of beer through the nation's approximately 500,000 retail outlets, BEVERAGE WORLD MAGAZINE (March 1979) shows the following:

Share of Beer Sales

Food Stores	64%
On-Premise	20
Liquor Stores	7
Other	9
TOTAL	100%

Similarly, SUPERMARKETING MAGAZINE reported that food stores took in 62 percent of all consumer dollars spent on beer and 92 percent of all off-premise beer sales. It adds that beer provided $7.3 billion in business, overall, and in $1 million supermarkets alone, beer accounted for almost $4 billion in sales.

TABLE 3
1980 BEER WHOLESALE SALES, STATE EXCISE TAXES &
TOTAL LICENSE FEES AND FEDERAL TAX COLLECTIONS ON BEER BY STATE
($000)

STATE	WHOLESALE SALES	STATE TAX COLLECTIONS	FEDERAL TAX COLLECTIONS
ALABAMA	207,750	55,362	144
ALASKA	35,000	3,392	4
ARIZONA	257,000	8,453	2,801
ARKANSAS	128,500	9,544	21
CALIFORNIA	1,897,750	38,521	110,649
COLORADO	248,500	7,882	124,197
CONNECTICUT	182,500	9,704	26
DELAWARE	48,500	1,231	2
DIST. OF COLUMBIA	50,500	See Md.	See Md.
FLORIDA	885,500	140,908	82,813
GEORGIA	333,000	101,199	60,718
HAWAII	77,750	8,678	32
IDAHO	75,250	3,420	11
ILLINOIS	892,500	20,703	28,174
INDIANA	376,500	17,395	11,454
IOWA	229,750	14,489	298
KANSAS	161,250	9,678	74
KENTUCKY	212,250	5,617	11,297
LOUISIANA	307,250	37,023	1,676
MAINE	86,000	7,530	20
MARYLAND & D.C.	383,500	15,681	15,704
MASSACHUSETTS	491,750	16,528	12,959
MICHIGAN	681,250	52,398	62,526
MINNESOTA	314,500	16,922	30,076
MISSISSIPPI	151,250	19,511	78
MISSOURI	375,750	7,416	104,520
MONTANA	83,500	4,403	245
NEBRASKA	134,000	6,076	3,404
NEVADA	92,250	1,777	2
NEW HAMPSHIRE	98,000	5,096	25,529
NEW JERSEY	506,250	6,050	62,021
NEW MEXICO	112,750	3,128	2
NEW YORK	1,215,500	24,679	115,352
NORTH CAROLINA	359,000	55,285	102,736
NORTH DAKOTA	55,250	3,191	8
OHIO	821,250	49,836	67,240
OKLAHOMA	188,750	18,940	161
OREGON	204,000	5,254	10,424
PENNSYLVANIA	970,250	32,749	52,777
RHODE ISLAND	77,000	1,671	5,905
SOUTH CAROLINA	208,250	47,712	33
SOUTH DAKOTA	50,250	4,802	44
TENNESSEE	280,250	55,359	18,518
TEXAS	1,339,750	75,021	141,276
UTAH	68,750	2,192	75
VERMONT	45,000	3,874	1
VIRGINIA	370,250	32,533	40,414
WASHINGTON	333,500	4,560	45,315
WEST VIRGINIA	109,000	6,654	59
WISCONSIN	501,500	10,183	186,011
WYOMING	47,750	1,229	26
	17,302,500	1,091,439	1,547,853

SOURCE: WHOLESALER SALES, BEVERAGE DATA BANK, BEVERAGE MARKETING CORPORATION: STATE TAX COLLECTIONS, INDIVIDUAL STATE TAX BUREAUS: FEDERAL TAX COLLECTIONS, U.S. TREASURY, INTERNAL REVENUE SERVICE.

THE 10 LEADERS IN STORE VOLUME

Rank '78	 '77	 '76	Item	1978 Grocery Store Sales (add 000)	% Change In Sales '78 to '77	% of Store Volume '78
1	1	1	Fresh Beef	$13,823,080	+20.1%	8.50%
2	2	2	Provisions	11,808,720	+14.2	7.26
3	3	3	Fresh Vegetables	11,084,790	+ 9.9	6.82
4	4	4	Beer	7,325,160	+ 7.9	4.50
5	5	5	Fresh Fruits	6,496,570	+10.7	3.99
6	6	6	Cigarettes	5,467,600	+ 7.7	3.36
7	8	8	Paper Products	4,588,850	+10.7	2.82
8	7	7	Fresh Milk	4,413,760	+ 4.5	2.71
9	10	10	White Bread	4,108,690	+12.8	2.53
10	11	11	Fresh Poultry	3,921,210	+17.1	2.41

Source: SUPERMARKETING, SEPTEMBER 1979.

These statistics clearly demonstrate that the food store is the major outlet for beer sales in this country. What, then, is the structure of the food outlet?

According to PROGRESSIVE GROCER, total grocery store sales in 1981 were approximately $241 billion. The 28,680 supermarkets in the country accounted for $171.6 billion, or 71 percent of dollar sales. Those supermarkets represented only 17 percent of all stores. Further, chain supermarkets which represented 11 percent of all grocery stores accounted for about 50 percent of all grocery store sales. The 1981 sales of the top ten publicly held chains totaled about $71.4 billion, or four times the total of the nation's 4,500 beer wholesalers. Similarly, the $71.4 billion of the top ten chains represent over 60 percent of all chain supermarket sales.

Thus, we have the beer wholesaler, who is bascially a small businessman, located between two increasing concentrating groups--brewers and food retailers. The wholesaler, relatively speaking, is without economic power in comparison with the brewer and his volume customer, the food store chain.

The Price of Beer Relative to Other Beverages

Recently, there has been discussion concerning the possible impact of the Malt Beverage Interbrand Competition Act upon consumer beer prices. Let us consider the history of beer pricing and past interbrand competition in the market place.

CONSUMER PRICE TRENDS FOR MALT BEVERAGES AND OTHER PRODUCTS 1965-1981

	Beer	Soft Drinks	Wine	Distilled Spirits	Coffee	Non-Alcoholic Bev.	All Items
1965	96.8	91.3	98.3	98.2	107.2	101.5	94.5
1966	98.3	94.2	98.8	98.8	105.3	100.9	97.2
1967	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1968	102.8	107.2	103.8	101.4	98.8	101.9	104.2
1969	105.4	112.7	108.2	102.5	99.0	104.6	109.9
1970	108.9	119.0	116.7	105.0	119.0	117.4	116.3
1971	112.9	125.9	122.3	106.4	121.8	121.6	121.3
1972	113.9	128.3	127.0	108.6	119.4	121.3	125.3
1973	115.6	131.7	135.2	109.2	135.0	130.2	133.1
1974	126.3	163.0	147.3	110.9	160.5	155.6	147.7
1975	140.3	200.5	154.0	114.1	172.9	178.9	161.2
1976	143.7	194.2	157.4	116.0	243.6	214.0	170.5
1977	145.9	203.4	161.9	117.5	451.2	322.4	181.5
1978	154.0	218.3	177.6	122.3	409.1	340.8	195.3
1979	170.0	239.1	193.6	127.3	385.5	357.8	217.7
1980	187.5	269.1	210.4	135.4	426.4	395.8	246.8
1981	201.0	296.9	226.1	143.0	353.4	412.6	272.4

Source: U.S. DEPARTMENT OF LABOR, BUREAU OF LABOR STATISTICS.

First, the table above demonstrates that interbrand competition in the beer industry has worked to the benefit of the consumer. While soft drink prices have increased by 225 percent since 1965, wine by 130, distilled spirits by 46, coffee by 230, non-alcoholic beverages by 307 (non-alcoholic beverages includes cola drinks, diet cola, other carbonated drinks, coffee and non-carbonated drinks) and all items in the Bureau of Labor Statistics price index by 188 percent--beer prices have risen by only 108 percent. The competition between the brewers, wholesalers and retailers in the United States and the resulting economies of scale together with sharp gains in productivity have enabled consumers to benefit in the form of price advantages while, at the same time, giving them a wide variety of brand availability.

Second, from 1971 to 1981, the consumer price of beer increased by an average of only 78 percent. In contrast, the Consumer Price Index jumped 124 percent, the cost of bread grew by 110 percent, soft drinks increased by 136 percent, utility rates climbed 202 percent and gasoline prices increased 287 percent. In fact, out of 121 consumer goods for which the Bureau of Labor Statistics has comparable figures, 83 percent registered a greater price increase over the 1971-1981 period than did beer.

It is important to note that the indices for alcoholic beverages (beer, wine and distilled spirits) shown above include as a part of the price measured, the increases in state and local excise taxes. These have increased dramatically for the 10 years covered by the table. That is to say, the price performance of alcoholic beverages is far more favorable to the consumer than the indices indicate because the amount of excise tax increases are reflected therein. In this regard, it should be noted that excise taxes on beer at the state and local level are being increased at a greatly accelerated rate. In virtually every state in the Union, there are current efforts to increase the excise tax on beer.

Third, let us consider price movement in the soft drink industry, which now has virtually the same exclusive territory law in effect as that presently under consideration for malt beverages.

The Soft Drink Interbrand Competition Act became effective in June 1980, and based on arguments presented at the time of hearings for that act, one might have expected soft drink prices to consumers to escalate specifically due to the act. The following table is offered for consideration.

Per Cent Change in Consumer Price Index for Soft Drinks, 1978-1981

PERIOD	% CHANGE
1978 January--June	4.5
July--December	2.7
1979 January--June	3.4
July--December	3.7
1980 January--June	7.3
July--December	6.3
1981 January--June	2.1
July--December	1.2

Source: U.S. DEPARTMENT OF LABOR, BUREAU OF STATISTICS

The foregoing table reveals, however, that prices in 1981 of soft drinks (cola, excluding diet) increased at a considerably lower rate than in previous times. Obviously, it cannot be maintained that there is a cause and effect relationship between the change in price movement and the Soft Drink Interbrand Competition Act. There are too many other variables impacting on price which could cause such a change in trends. We do, however, suggest that prices have not increased abnormally since the Act became effective (actually, the rate of increase sharply declined), and those who predict price increases as a direct result of the Interbrand Competition Act should reconsider their contentions in view of this "real world" data.

Statement
of
James L. Tito
Latrobe Brewing Company

Mr. Chairman and Members of the Committee:

My name is James L. Tito. I am Vice-President of the Latrobe Brewing Company, a mid-size brewery located in Southwestern Pennsylvania. I appear before you today in support of S. 1215, the Malt Beverage Interbrand Competition Act.

The desire of the Latrobe Brewing Company to see the legislation passed is based on considerations different, in some respects, from those espoused by our larger competitors. The reason for this is quite simple. Because our volume is a fraction of the larger brewers and the number of brands is limited, we have far more at stake if the consumer does not receive a fresh, quality beverage. This can be seen more clearly by examining the trends in the malt beverage industry over the past few years.

In both the case of the brewer and the retailer, there has been increasing concentration even within the past five years. Thus, while in 1975 the top five brewers produced 66% of total beer sold in this country, in 1981 that figure was almost 75%. Similarly, with respect to retailers, the ten leading publicly held nationwide supermarket chains represented 65% of that category's sales in 1975, while in 1980 that figure had risen to 70%.

Standing between these two highly concentrated elements of the malt beverage distribution system is the beer wholesaler or "distributor." He is usually a small businessman. In 1979 (the most recent information available by size) almost 26% of the nation's wholesalers employed between 1 and 4 people, 75% of beer wholesalers have less than 20 employees.

Because of this relatively low concentration, the distributor has been the most effective force in promoting interbrand competition in the malt beverage market in the United States. That competition has worked directly in the interest of consumers.

Another consideration is that brewers can best secure a high quality of sales and service to all retailers through an assignment of distributors to specific areas, thereby making the distributors responsible for all accounts in that specific geographic area. The reward of such an assignment is the opportunity to secure the patronage of the large retailers; with this reward goes the obligation of service to the smaller accounts. The continued calling on retailers, both on and off premise, is vitally important to obtaining distribution of products of smaller brewers.

Competition between brands and other products, such as wine and liquor, furnishes an additional incentive for all distributors to service all accounts in the best manner possible.

Success only follows repeated retailer calls by an effective wholesaler sales force. Transshipping usually only carries our products as far as the retailer's doorstep, delivering rather than selling.

While loss of wholesaler services hurts all brewers, we think that transshipping hurts smaller brewers the most. The success of the brands of small brewers is dependent upon their ability to react to momentary changes in demand which can only be serviced by wholesalers, who are secure in the knowledge that the customers they are soliciting as retailers are their customers today and will be their customers tomorrow.

Lacking large impact advertising budgets, the brands of small brewers are normally not the first call of consumers and retailers. Most often they are sold by either availability or by continued suggestion of the wholesaler to the retailer. This form of service or selling will only be effective when the wholesaler and his employees are secure in the knowledge that the investment they make in both time and dollars for sale promotion will be rewarded by the ability to service the account when it does begin buying.

The distributor's relationship with a retailer outside of his primary area of responsibility is often short-lived and the business is lost for one reason or another. This is not a significant loss to the distributor, as he may go about his business elsewhere and the retail account was marginal at best, in the first place. However, as to manufacturers, the loss tends to be long-term for the brand and it may be permanent because of the ill will which has been generated between the retailer and, what are now, two former distributors, that is, the distributor within the retailer's area of primary responsibility and the transshipping wholesaler.

A system of exclusive territories promotes accountability, not only to the brewer, but also to the consumer. Since the authorized distributor would be responsible for selling all of his brewer's products in his assigned territory, he would also be responsible to ensuring the freshness of all those products. Without exclusive territories, however, no brewer is able to guarantee that the beer consumed is always his best; as a result, both the brewer and the consumer suffer.

In addition to promoting product quality, exclusive territories encourage distributors to service all retailers in their marketing area, all of the brands and sizes available, rather than concentrating on just the most profitable one. In most cases, if not all, the beer that is transshipped is normally packaged in non-returnable containers. This might not necessarily be the product being consumed in the market area and the brewer eventually will find that he has no market at all when he attempts to sell a product unadvertised without support in the improper package.

In order to succeed in this fiercely competitive market, distributors must do much more than simply sell beer. They must provide many services which enhance the image of the brands they carry, even when such services in and of themselves do not return high profits.

Distributor efforts benefit the brewer, retailers, consumers and the community at large. Without exclusive territories, however, transshipping wholesalers receive a free ride on an authorized distributor's efforts to promote goodwill for the brewer's products in his market. No distributor can or should be expected to subsidize transshipping intrabrand competitors in this manner.

Finally, I would note that exclusive territories would benefit small, regional brewers even more than national brewers. All brewers need distributors who will devote their energies to marketing the brewer's products aggressively. Unless they can offer distributors an exclusive territory, those brewers with relatively small volume may have difficulty attracting or retaining competent and aggressive distributors who are willing to invest the time, money and effort necessary to make that brewer's brands a viable force in the marketplace.

Senator SIMPSON. It is very interesting to have your views. It is a tough issue. There are a lot of cosponsors including myself wanting to do the appropriate thing to see that we preserve and protect a very important industry in America.

I will have a moment now for a question or two of my own. I will submit further ones in writing. Having a great interest in this area when I was younger and weighed 260 pounds and was sustained on beer, I thought beer was food when I was 21 and became a connoisseur.

I want to ask you, Mr. Sellinger. Is it not true that when some brewers and distributors have entered into exclusive territorial arrangements that have been upheld by the courts after applying this so-called rule of reason test of those arrangements that has occurred, the courts have upheld that. Yet, opponents of this legislation claim that the rule of reason is a sufficient method of testing these arrangements without any passage of any legislation to create that rule. How do you respond to that argument?

Mr. SELLINGER. I guess the rule of reason brings on lawsuits. Wholesalers, and there are numerous small wholesalers, could not afford lawsuits; nor do brewers want to become involved in a lot of lawsuits because they are just too expensive. Sometimes we have seen decisions under the rule of reason, where there have been judgments made and then have even been appealed after that. So, there are unending lawsuit costs.

Senator SIMPSON. Mr. Tito, you speak with emphasis about freshness. I know of your product, have sampled it, extraordinary suds. Could not the use of freshness dates lessen the concerns over quality control? That has been discussed several times. It is in the testimony, where we have talked about dates, freshness, expiration of quality, and so on.

Mr. TITO. They can be used. But in many cases these would turn out to be very punishing to the distributor himself. Beer that is moved into his market area which might be transshipped in becomes his responsibility. The man who is the transshipper loses that responsibility. The poor distributor who happens to be in an area, where large accounts might receive the transshipped beer is then stuck with it. He would have to then take that beer back from a retailer. He would be at a financial loss.

Senator SIMPSON. And yet freshness is a very important part of the marketability of beer.

Mr. TITO. Freshness is the key to marketability of beer. We found in looking over the years in taking product from the retail shelves that one could walk into a market, randomly sample products that are there, and find age differences of 100 days between the most recent arrival and one that seems to have been there for some time.

Senator SIMPSON. Mr. Pohl, you asserted there moments ago that the current system works.

Mr. POHL. Yes, sir.

Senator SIMPSON. Does that indicate that State law then may be adequate as it exists without S. 1215? I would like your comments on that.

Mr. POHL. I think the threat that is implied currently to us as a small brewer is what we are concerned about. The system as it is right now in Ohio works and works very well. The implied threat to that current system is what we are concerned about. As a small company, we cannot afford to get involved in large lawsuits over wholesaler functions and related items like that. It would immediately tie us up and tie all our efforts up.

One of our biggest problems is lack of manpower. We operate with a marketing staff of really three people. If you start tying up our marketing staff in law-related functions, we lose everything, all the momentum we have got going.

Senator SIMPSON. There is an argument proposed, as I have reviewed the materials prior to this hearing, where we say there are other industries that market perishable products. The question then arises what would make the beer industry different from, say, the dairy industry or the produce industry, which also market perishable products and which seem to prevail without any legislation of this type. It was stated that, if we were to pass legislation, that these other industries would want special attention and special consideration. I would like your comments as you build your record.

Mr. SELLINGER. The other industries are not regulated like the brewing industry or the liquor industry by State regulations. The State has its own regulations, and we have to abide by those individual State regulations.

Senator SIMPSON. Do you have any comment on that?

Mr. TITO. The freshness of beer has been a function of the brewer, the distributor, and the retailer over the years. The freshness of milk has been something that we all grew up on. Everybody put a date on a milk carton. That was passed by somebody hundreds of years ago. Beer has always been an implied system where we trusted each other and we all exerted our best effort to take beer from the brewer, through to the distributor, and to the retailer so the consumer got the best value for the money they were paying.

Mr. POHL. Senator, I have gone into large retail accounts and found beer well over 100 days old. You know, if it was already being done, I think that would be one thing; but it is not currently being done.

Senator SIMPSON. Well, it is an interesting issue, especially, I think, in the area of dairy products where you have a mysterious system of marketing orders which would boggle the mind when you talk about regulation.

That is helpful. I appreciate very much your testimony. I thank you for your appearance.

Mr. POHL. Sir, can I have one last comment?

Senator SIMPSON. Yes.

Mr. POHL. In the State of Indiana, as an example of a small brewer, what S. 1215 means to us. I have in front of me State shipments, import sheets basically, of beer shipped into the State. It is cumulative through February 1982, so it is only a 2-month report. But the top eight brewers are listed on this sheet, and then all others are combined, which is basically your smaller brewers. The all-other segment is down 29.7 percent in the State of Indiana. That simply means that the large national brewers are getting their beer transshipped, but the little guy is out in the cold.

Senator SIMPSON. That indeed is a national trend in the last 20 years. It has been quite startling how many local breweries have gone out of existence. Is that not a sizable percentage?

Mr. POHL. I think that has been a trend. Yet, in the State of Ohio, which is right next to it, in the borders in Ohio, our sales are up.

Senator SIMPSON. Is this part of the record? Would you like to enter that?

Mr. POHL. I have a sheet right here on Indiana if you care to have it.

Senator SIMPSON. Without objection, we will insert it.

[Material referred to follows:]

STATE SHIPMENTS BULLETIN APRIL 8, 1982

INDIANA

SHIPMENTS OF MALT BEVERAGE, IN BARRELS

CUMULATIVE THROUGH JANUARY 1982

LEADING BREWERS	PACKAGE	% CHNG	DRAFT	% CHNG	TOTAL	% CHNG	YTD	% CHNG
ANHEUSER-BUSCH, INC.	41,850	3.2	9,329	12.4	51,179	4.7	51,179	4.7
MILLER BREWING CO	54,921	1.9	8,555	46.6	63,476	6.3	63,476	6.3
PABST BREWING CO.	37,648	17.8-	3,287	19.8-	40,935	18.0-	40,935	18.0-
THE STROH BREWERY CO.	26,565	32.5-	3,798	4.6	30,363	29.4-	30,363	29.4-
G.HEILEMAN BREWING CO., INC	21,353	12.1	2,072	49.4	23,425	14.7	23,425	14.7
OLYMPIA BREWING CO.	9,777	43.6	1,015	8.1-	10,792	36.4	10,792	36.4
JOS. SCHLITZ BREWING COMPANY	6,068	75.3	325	22.3-	6,393	64.8	6,393	64.8
FALSTAFF	3,634	8.3	181	2.3	3,815	8.0	3,815	8.0
ALL OTHER BREWERS	2,895	39.1-	187	.5	3,082	37.6-	3,082	37.6-
TOTAL	204,711	5.7-	28,749	14.4	233,460	3.6-	233,460	3.6-

INDUSTRY TOTAL	PACKAGE		DRAFT		TOTAL
YEAR TO DATE	204,711	5.7-	28,749	14.4	233,460

SOURCE: INDIANA OFFICE, U.S. BREWERS ASSOCIATION, INC. SUMMARY OF BREWERY SHIPMENTS AND TAXES COLLECTED. INCLUDES SALES TO MILITARY INSTALLATIONS.

STATE SHIPMENTS BULLETIN MAY 3,1982

INDIANA

SHIPMENTS OF MALT BEVERAGE, IN BARRELS

CUMULATIVE THROUGH FEBRUARY 1982

LEADING BREWERS	PACKAGE	% CHNG	DRAFT	% CHNG	TOTAL	% CHNG	YTD	% CHNG
ANHEUSER-BUSCH, INC.	43,879	16.6	7,981	2.3-	51,860	13.2	103,039	8.8
MILLER BREWING CO	73,294	15.4	8,792	25.2	82,086	16.4	145,562	11.7
PABST BREWING CO.	29,838	10.5-	3,308	5.1-	33,146	10.0-	74,081	14.6-
THE STROH BREWERY CO.	33,256	8.4-	2,974	24.9-	36,230	10.0-	66,593	20.0-
G.HEILEMAN BREWING CO., INC	20,117	2.6-	1,402	.6-	21,519	2.5-	44,944	5.8
OLYMPIA BREWING CO.	6,792	10.1-	1,131	22.8-	7,923	12.1-	18,715	10.5
JOS. SCHLITZ BREWING COMPANY	6,822	97.7	415	22.0-	7,237	81.7	13,630	73.4
FALSTAFF	2,882	42.8-	139	23.6-	3,021	42.1-	6,836	21.9-
ALL OTHER BREWERS	2,886	20.9-	167	20.1	3,053	19.4-	6,135	29.7-
TOTAL	219,766	4.1	26,309	.2-	246,075	3.6	479,535	.0

INDUSTRY TOTAL	PACKAGE		DRAFT		TOTAL
YEAR TO DATE	424,477	.9-	55,058	6.9	479,535

SOURCE: INDIANA OFFICE, U.S. BREWERS ASSOCIATION, INC. SUMMARY OF BREWERY SHIPMENTS AND TAXES COLLECTED. INCLUDES SALES TO MILITARY INSTALLATIONS.

STATE SHIPMENTS BULLETIN · JUNE 2, 1982

INDIANA

SHIPMENTS OF MALT BEVERAGE, IN BARRELS

CUMULATIVE THROUGH MARCH 1982

LEADING BREWERS	PACKAGE	% CHNG	DRAFT	% CHNG	TOTAL	% CHNG	YTD	% CHNG
ANHEUSER-BUSCH, INC.	62,389	24.8	10,985	1.6	73,374	20.7	176,413	13.5
MILLER BREWING CO	96,791	7.8	11,948	23.4	108,739	9.3	254,301	10.7
PABST BREWING CO.	48,552	13.8-	3,868	16.0-	52,420	14.0-	126,501	14.4-
THE STROH BREWERY CO.	42,912	27.2-	4,850	4.8-	47,762	25.4-	114,355	22.3-
G.HEILEMAN BREWING CO., INC	31,454	2.1	2,640	8.7	34,094	2.6	79,038	4.4
OLYMPIA BREWING CO.	13,658	26.7	1,569	28.1-	15,227	17.5	33,942	15.5
JOS. SCHLITZ BREWING COMPANY	9,838	97.9	717	9.4-	10,555	83.2	24,185	77.5
FALSTAFF	4,718	14.8-	316	45.6	5,034	12.6-	11,870	18.2-
ALL OTHER BREWERS	5,105	9.2	269	35.2	5,374	10.3	11,509	15.4-
TOTAL	315,417	1.1	37,162	3.2	352,579	1.4	832,114	.6

INDUSTRY TOTAL	PACKAGE		DRAFT		TOTAL
YEAR TO DATE	739,894	.0	92,220	5.4	832,114

SOURCE: INDIANA OFFICE, U.S. BREWERS ASSOCIATION, INC. SUMMARY OF BREWERY SHIPMENTS AND TAXES COLLECTED. INCLUDES SALES TO MILITARY INSTALLATIONS.

Senator SIMPSON. Thank you very much.

The final panel is Mr. Doug Simmons, Free Enterprise Liquor Dealers, Indianapolis; Joseph Lackey, president of the Indiana Retail Grocers Association; and Richard Quinn, the Indiana Malt Beverage Association.

Please proceed in that order. I do again remind you of the time limitation. I regret that but it is a necessity. Mr. Simmons please.

Mr. LACKEY. Mr. Chairman, my name is Joe Lackey, and they have asked if I could go first. I will be very brief.

Senator SIMPSON. That is perfectly appropriate.

Mr. LACKEY. I have one of those famous transshippers here with me, and I would like to give him maximum opportunity to defend himself here in just a few moments.

Senator SIMPSON. I see he does not have a cloak over his head. May we please have order in the hearing room? Please proceed.

STATEMENTS OF A PANEL CONSISTING OF JOSEPH A. LACKEY, PRESIDENT, INDIANA RETAIL GROCERS ASSOCIATION; DOUGLAS J. SIMMONS, FREE ENTERPRISE DEALERS, INC.; AND RICHARD M. QUINN, VICE PRESIDENT, INDIANA MALT BEVERAGE ASSOCIATION

Mr. LACKEY. Mr. Chairman, the Indiana Retail Grocers Association represents over 3,000 grocers and over 40,000 food store employees around the State. These are all types and sizes of operations: national chains, small convenience stores, independent operators, and, of course, your famous mom and pops. So, we are involved with all different sizes and types of operations.

S. 1215, the Malt Beverage Interbrand Competition Act, is what we call in Indiana the beer baron bill. We coined that phrase there. It was the rule that we operated under from 1933 until 1974. Consequently, that is why we have asked to be here today, to explain to you the effects of that rule in Indiana and upon our Indiana retailers.

I would like to just very briefly picture three situations for you.

It is Friday afternoon and the grocery store is packed. People are doing their weekly shopping. A beer truck pulls up out front, and the driver wheels in a load of popular brand beer and sets it at the front of the store behind the cash registers, obstructing the traffic flow. He leisurely walks to the office and presents an invoice and demands payment. The store manager protests that he needs the product in the back room and not in the front of the store. The beer wholesaler representative informs the manager that, if he wants it moved, he can move it and again demands payment. The store manager has no alternative. He pays and hurries to get the beer out of the congested area and restock the shelves.

Another situation: It is Saturday morning and the store is on the verge of running completely out of its best-selling brand of beer. A hasty call is put in to the local wholesaler who responds that the beer will be delivered on Monday, the regular delivery date. The manager is faced with a stockout and no alternative. He cannot go and buy the beer and haul it himself. He cannot even transfer it from another store under common ownership.

The final situation: A retailer is being charged twice the price of his largest competitor who happens to be located just across the county line—and in Indiana that was a different territory—and, consequently, has a different beer wholesaler. He protests to his wholesaler that the high prices are not allowing him to be competitive and, therefore, he is losing customers. To which the wholesaler responds, "That's tough."

These situations I have described to you are not fantasy. They were the rule in Indiana, and it was only when situations got this bad that finally the beer baron died. Since that time, we have gone to a competitive wholesaling situation which has resulted, as was reported to you earlier and as was documented in the interim study committee by the State of Indiana this last summer on alcoholic beverage, a 20-percent reduction in price of beer to the consumer initially upon the passage of the law.

We estimate, too, in that interim study committee that, if the beer baron goes back into effect, we would expect to see at least a 25-percent increase.

That brings us to our concern for this bill. As recently as 3 months ago, we were involved in an attempt to repeal the existing rule, which bans beer baron territories from Indiana. We were successful in that, in keeping that rule in effect. However, we know that, if this bill passes, it will provide the impetus for them to come back and attempt to repeal that rule again. That is why this bill is so important to those few wholesalers in Indiana who still want to maintain the beer baron bill and the fixed territorial system.

It is not part of my prepared text, but there has been a lot of comment here about the soft drink bill. I will be happy to answer any questions you might have about it.

Let me say, however, that the retail grocers in this country, especially in Indiana, anywhere in the Midwest, are suffering a great deal under this bill. There is a great deal of inequity. We have been in contact with the Federal Trade Commission on several occasions about various incidents. They basically say there is nothing we can do about it, that arbitrary territories have been established by law. The same type of situation that we had under the beer baron is now taking place in the soft drinks. It is not a good bill. So, those that hold that up as an example of the basis for the need for this law are using a bad example. We can provide you with any additional information you might require on that bill.

I will be followed, Mr. Chairman, if there are no direct questions, by Mr. Doug Simmons.

Senator SIMPSON. Please, Mr. Simmons, if you will.

Mr. SIMMONS. Thank you, Senator.

Senator SIMPSON. Without objection, Mr. Lackey's prepared statement will be inserted.

[Material referred to follows:]

STATEMENT OF JOSEPH A. LACKEY
President
Indiana Retail Grocers Association
BEFORE THE SENATE JUDICIARY COMMITTEE

Mr. Chairman/Members of the Committee:

My name is Joe Lackey and I am the President of the Indiana Retail Grocers Association (IRGA). IRGA represents over 3,000 grocery stores and their over 40,000 food store employees located throughout the state of Indiana. Our membership includes national corporate chains, independent operators, convenience stores and the classic single store "mom and pop" type operations.

S. 1215 - "Malt Beverage Interbrand Competition Act" is what we call in Indiana the "Beer Baron Bill". It was the rule in Indiana from 1933 (when the original Alcoholic Beverage Act was enacted) until 1974. Consequently, we feel that Hoosiers are uniquely qualified to address this issue since we have, in fact, seen it both ways.

Picture these situations:

It's Friday afternoon and the grocery store is packed - people are doing their weekly shopping. A beer truck pulls up out front and the driver wheels in a load of popular brand beer and sets it at the front of the store behind the cash registers - obstructing the traffic flow. He leisurely walks to the office and presents an invoice and demands payment. The store manager protests that he needs the product in the back room and not in front of the store. The beer wholesaler representative informs the manager that if he wants it moved he can move it and again demands payment. The store manager has no alternative - he pays and hurries to get the beer out of the congested area and restock the shelves.

Another situation - *It's Saturday morning and the store is on the verge of running completely out of its best selling brand of beer. A hasty call is put into the local wholesaler who responds that the beer will be delivered on Monday (the regular delivery date). The manager is faced with a stockout and no alternative. He can't go and haul the beer himself. He can't even transfer it from another store under common ownership.*

And the final situation - A *retailer is being charged twice the price of his largest competitor who happens to be located just across the county line (a different territory) and, consequently, has a different beer wholesaler. He protests to his wholesaler that the high prices are not allowing him to be competitive and, therefore, he is losing customers. To which the wholesaler responds, "That's tuff".*

These situations that I have just described for you are not fantasy. Each of these, and at times worse, were the norm for Indiana retailers in the years that we operated under the Beer Baron. There is no reason to believe that Indiana wholesalers and their brewers are different from any others in the nation. Consequently, what happened in our state under exclusive territories will happen to the nation if S. 1215 becomes law.

The question of controlled territories for beer wholesalers is one which impacts our industry directly. Ninety-two percent (92%) of all malt beverages sold for off-premise consumption is sold by grocery stores. Consequently, we are vitally concerned about the outcome of this question. When controlled territories were the rule for our Indiana retailers and, consequently, our customers (the citizens of Indiana), they both suffered greatly. We suffered because we had no alternative seller or supplier of alcoholic beverage products to our stores. This situation would be analogous to you as a customer being able to shop at only one store. If you were unhappy with the services, hours or prices at that particular store, you would have absolutely no option. I think that you can see that the store also would have no incentive to provide you with products and services at a price and in a manner that you desire. This is the same situation that we had under the controlled territories or Beer Baron law. It also is the same situation that we will have under S. 1215. In many cases, beer deliveries to the store were irregular and often incorrect. At the same time, shortages occurred regularly because wholesalers refused to respond to special orders or unusual situations.

Also, there is documentable evidence that everyday shelf prices have dropped since the demise of the controlled territories or the beer barons. This has happened because of increased competition at the wholesale level accompanied by corresponding shrinks in profit margins and heavy competition at the retail level.

Contrary to the impression that you may have been given, the majority of beer is not being provided by out of territory wholesalers or as they are commonly referred to "trans-shippers". The availability of the trans-shipper, however, has caused local suppliers or wholesalers to respond in a much more positive manner to their customers, the retailers. Deliveries are now on time and correct. Wholesalers readily respond to special situations and deliveries. We feel that this situation exists simply because of the availability and the existence of the trans-shippers. Now it is important for the wholesaler to treat the retailer in the same manner in which the retailer treats his customers. For the first time, we have alternative sources of supply. A return to a controlled territory or passage of S. 1215 will eliminate this situation and put us back to being dictated to by the local wholesalers.

Wholesalers and brewers continually bring up limited shelf life as a reason for their need for controlled territories. Retail grocers keep beer on their shelves from 14 to 30 days. Consequently, beer with a 75 to 120 day shelf life is not being placed in any type of peril by the rotation rate of the supermarkets and grocery stores. Additionally, product quality and the need for rotation is an integral part of the daily operation of the supermarkets. As you well know, many of our products are much more sensitive to deterioration (i.e. produce, meat, dairy, etc.).

For all of these reasons, we are very much opposed to the passage of S. 1215 or in any way imposing or allowing for the imposition of controlled territories in the beer distribution industry. Additionally, there are other factors that need to be considered.

Much of the food distribution industry is watching your actions on controlled territories for beer wholesalers. They are watching to see what precedent is set. Specifically, wholesalers, such as, small dairies and bakeries could conceivably ask the Congress to provide for them a controlled market. Their plight is not unlike that of the beer wholesalers. They have no guaranteed sales and at the present time the highly competitive nature of the distribution industry is causing some hardships. We think that it is important that you be aware of this. The establishment of controlled territories for beer wholesalers will undoubtedly cause an endless stream of other wholesalers and suppliers seeking congressional relief.

Many businesses in this country succeed and fail daily without seeking or receiving congressional attention. A good example is the grocery industry. At the end of World War II there were over 1400 grocery stores in the city of Indianapolis. Today, by using your imagination and counting every fruit stand, convenience store, mom and pop operation and supermarket, you would be lucky to come up with 500. Yet the Indiana Legislature and the U.S. Congress took no action, nor were they asked to, to save those operators. We think that this is as it should be. Business must be based on its individual ability to supply a product and service in a way and at a price that is acceptable to its customers. This is true of wholesalers as well as retailers.

Proponents of S. 1215 will argue that without legislation some beer wholesalers will go out of business. Based on what has happened in Indiana this is probably true. When the Beer Baron Law was in effect and controlled territories were the rule, there were over 200 beer distribution companies located throughout the state. Over 200 companies to supply the beer consumed by the citizens of Indiana. Compare this with the fact that there are only 13 full-line grocery warehouses in or around the state which supply all of the state's over 4,000 retail grocers which, in turn, supply all of the state's consumers. Each of those stores will average over 15,000 items which they provide to the consumer on a regular basis. Retail operators are free to change wholesalers in order to secure the best possible price and service for their customers. The result is the most competitive manufacturer, wholesaler and retailer pricing structure of any industry in the world. No other industry operates on an average of less than one-percent (1%) profit. We feel that it is time that the beer wholesalers learn how to run their businesses in an efficient and competitive manner.

In summary, upon passage of S. 1215, the breweries will establish contractually their exclusive territories. Retailers will have one supplier of each brand and will not be allowed to purchase from any other. Beer prices to consumers will increase by at least twenty-five percent (25%) immediately upon the establishment of these territories. Consumers will be outraged at these increases, but they, like the retailer, will have no alternative. Beer wholesalers will fix prices and continually avoid any type of competitive situation. Brewers will cause prices to fluctuate only to obtain additional shares of a specific market, and once a dominant share of the market has been obtained prices will again increase substantially. Free enterprise will be lost in the beer distribution industry. Small wholesalers will never have the opportunity to become larger. They will have a fixed number of customers with no opportunity to compete for additional ones. All incentive to keep prices low and to operate efficient distribution centers will be lost. Prices will steadily increase to the beer consuming public and there are a lot more beer drinkers than there are beer wholesalers.

I appreciate the opportunity to present this testimony to you today and stand ready to answer questions and provide information that you may desire.

Respectfully Submitted,
Joseph A. Lackey
Joseph A. Lackey, CAE
President

ADDENDUM

RESPONSES OF THE RETAIL GROCERS TO BEER WHOLESALER'S ARGUMENTS FOR PASSAGE OF S. 1215

Note: Statements shown in italics are from Beer Wholesalers and were made as justification for passage of the Malt Beverage Interbrand Competition Act (Beer Baron Bill). Responses are made by the Indiana Retail Grocers Association.

Barons Say: It would enhance competition on the local level by having more competition from other small distributors.

Response: This bill would totally eliminate competition by again forcing retailer and dealer permittees to purchase from specific beer wholesalers. There may be more than one wholesaler in many territories, however, these wholesalers do not overlap on product carried. Consequently, if a dealer or retailer permittee in X territory wants to buy X brand beer there is only one wholesaler in that territory which can provide the product. If the law goes through it will eliminate any kind of competition by forcing purchases from that wholesaler only.

Barons Say: It would protect small business persons from being unfairly pushed out of business by large, heavily funded organizations.

Response: The key word in this argument is protect, which is exactly what the Beer Baron Bill would do - it would totally protect beer wholesalers by forcing retailer and dealer permittees to purchase only from the wholesaler within their territory regardless of price or service.

Barons Say: It would benefit the small retailers who would be forced out of business by having only one or two large distributors in a state, who sell only to the high volume retailers.

Response: The bill would significantly hurt small retailers. The competitive cycle is passed along through the various distribution points. If wholesalers are competitive, this encourages competition at the retail level. If you eliminate competition at the wholesale level, then the small retailer cannot afford to subsidize the cost of the product and may have to sell it at a higher rate than the high volume retailer, which has more funds available to subsidize the sale of the produce. In other words, it is easier for the large retailer to put items on sale that it is for the small retailer, especially when the prices are fixed for both.

The situation at this point is that a small retailer has the option of going to a more competitive wholesaler to buy a product and can shop for the best bargain. This bill, of course, would eliminate that option.

Barons Say: We feel that - if small distributors are forced out of business and the state is served by only one or two large distributors - prices will go to extraordinary high levels due to the lack of competition.

Response: It amazes one to understand how eliminating competition, which this bill will do, is going to force lower prices.

Barons Say: Small wholesalers have invested untold amounts of money in their local businesses - creating local jobs and enhancing the local tax income.

Response: All businessmen, large and small, invest a great deal of money in their businesses. Beer wholesalers must understand that in a free market there are no guarantees. There are no laws in Indiana or in the Nation which guarantees the profits of grocery stores, drug stores, liquor stores, taverns, department stores, clothing stores or any other retail segment of business with the exception of public utilities. As far as jobs created, the number of jobs in the retail grocery industry far exceeds all other segments of the Alcoholic Beverage Distribution System combined. There are over 70,000 jobs in the retail food outlets in Indiana alone.

Barons Say: With this legislation local wholesalers can and will continue to invest more money in their business and local community.

Response: We don't disagree with this - they will do something with the money to avoid the high taxation caused by the extremely high income they would derive from the passage of such a measure. By the same token, the defeat of this measure will also cause reinvestments in the business to keep the beer wholesalers competitive.

Barons Say: This legislation can cause small retailers and consumers a more fair and lower price for the product by creating more local competition.

Response: This argument is absurd. How can the total elimination of competition at the wholesale level guarantee a fair or lower price for consumers. One simply needs to look back a few years ago when the Beer Baron Philosphy was a reality in Indiana and compare those prices to todays market. Prices are substantially lower.

Barons Say: Wholesalers who operate out of their local area have to offer discounts on large orders that only large retailers can buy and, therefore, it becomes more difficult for the small retailer to compete.

Response: Response to the third statement really applies here again. This situation would not change under the new Beer Baron Bill. What would change is the ability of the local retailer to go elsewhere to find a more competitive supplier of the product.

Barons Say: We feel that this legislation also will prevent a monopoly from being formed by big business and, therefore, will cause a more equal and fair distribution to all concerned.

Response: The Beer Baron Bill is no argument against the formation of a monopoly. Such an illegal action could take place right now. In fact, where a controlled distribution system exists as under a Beer Baron Bill it is much easier to control the industry through the input of large investors. The fact that the industry is open to competition will allow for the continuation of that competition. We know from history that the competition will be there. The idea that a monopoly could be formed is ridiculous in light of current Federal Trade Commission and State Anti-Trust Laws which are in place.

Barons Say: In summation - we feel that we do not need another monopoly in the state of Indiana.

Response: Those of us who believe in free enterprise agree completely with this statement. We feel that what the Beer Baron would create is a monopoly on the part of the beer wholesalers. That is, total control of the sale of beer at wholesale by a close knit industry which has agreed to eliminate that competition and attempts continually to structure itself along those lines. A free and open market is opposed to only by those who are unwilling to compete.

Mr. SIMMONS. Mr. Chairman, my name is Doug Simmons. I am from Indianapolis, Ind. I am here today representing Mr. Mark McAlister. Mr. McAlister represents Big Red Liquors stores, which operate four liquor stores in Bloomington, Ind.

He is also a member of the Free Enterprise Dealers, Inc., a trade association of liquor store owners and operators scattered throughout Indiana.

As an individual operator and as a member of Free Enterprise Dealers, Inc., Mr. McAlister wanted me to relate to you his experience because he has had the opportunity to operate under both systems. In the good old days, as Mr. McAlister refers to it, the local distributors in his market operated as follows. One, they took retail sales on Monday, delivered on Tuesday and Wednesday, closed early on Wednesday, delivered on Thursday and Friday mornings, and closed early again on Friday. Saturday mornings were reserved for retail keg sales to consumers.

They now argue that exclusive territories are needed to insure freshness. But during the good old days, they did not check code dates in his stores.

Big Red Liquors did not receive any benefit from promotional discounts routinely offered to the wholesalers by the breweries.

The prices offered by the local wholesalers on comparable packages and brands were virtually identical.

In the current market system, Mr. McAlister's Big Red Liquors was the first to take advantage of the emergence of price competition in the wholesale level by sending their trucks to pick up beer at the wholesalers' docks. This was temporarily prohibited. So, they were then among the first again to get delivery from a transshipper. At that time, he saved an average of 50 cents to $1.50 per case under the local wholesalers' prices.

The reaction by his wholesalers: One, they raised their prices to their other customers to offset their loss; two, persons believed to be employees of one of the wholesalers smashed headlights and slashed tires on his trucks and harassed employees.

Also, they solicit kegs. They now heavily solicit keg sales on the Indiana University campus. And they sell kegs at a price lower than which they will sell to the retailer.

Their business, incidentally, is suffering.

Another distributor within Monroe County, on the other hand, reacted in a progressive manner. He is now handling Mr. McAlister's best line of beer.

Next are the benefits of competition. He has employed extra people whose primary responsibility is to rotate their beer. The jobs being claimed lost by the old-line wholesalers who do not want to compete are being picked up by store employees and the transshippers. As a result of the heavy competition now, they must have product freshness. They are concerned about it. It is not just the brewers who have that concern.

Most importantly, they are passing their savings on to their customers. In his testimony before the alcoholic beverage commission, Mr. McAlister said: I have yet to hear a consumer complain about the lower retail prices brought on by competition. None of the customers have suggested to us that we buy beer locally and raise their prices in order to cover the increased costs.

Likewise, even small retailers can take advantage of the savings being offered by competitive wholesalers. Competition gives small retailers the opportunity to expand if they so desire. He started off as a mom and pop operation but by using modern business practices and taking advantage of cost savings offered by the competition at the wholesale level he has grown.

Competition is keen among the various types of retailer permittees. There is utterly no reason that wholesalers should not be expected to do the same. Competition has brought the beer industry out of the dark ages, and it must be preserved for the good of the entire State.

In summarizing, Mr. Chairman, the feelings of Mr. McAlister and the Free Enterprise Dealers, I would like to say that it is simply nothing more than an economic war, with one segment of an industry asking the Government to intervene and provide guaranteed profit margins for them. The wholesalers who support this legislation, who have supported this legislation in Indiana are principally those who are in economic trouble due only to their poor business judgment and their steadfast refusal to compete. No one should have the right to be inefficient and noncompetitive in a market of captive consumers who pay whatever they are told to pay. Antitrust laws make it possible for each State to make their own decisions. The 21st amendment offers that.

I have heard it said I don't know how many times that it is a clarification of the 21st amendment. Yet, the author of the legislation and several others have said that this bill is clearly in the 21st amendment that the States have this right. I do not know why we have to clarify it if it is clearly there.

If this sort of economic feudalism is to become the rule, it should be the result of direct affirmative action by each State legislature and not by the Federal Government.

The proposed legislation is sometimes touted as promoting free enterprise. The legislation only gives freedom to brewers and the wholesalers to carve out protected preserves. Wholesalers would also be free of any incentive to adopt efficient business practices or provide good service to their customers.

The retailers have two equally undesirable choices: grin and bear it or go without.

I will be happy, Mr. Chairman, to answer any questions. A copy of my formal testimony which includes all of the parts has been submitted.

Senator SIMPSON. Fine. Thank you. Without objection, that indeed will be made part of the record.

[Material referred to follows:]

STATEMENT IN OPPOSITION TO
SENATE BILL 1215
DOUGLAS J. SIMMONS

My name is Douglas J. Simmons and I am from Indianapolis Indiana. I am here today representing Mr. Mark A. McAlister who had planned on being here today but at the last minute had to change those plans. Mr. McAlister represents Big Red Liquors which operates four liquor stores in Bloomington, Indiana.

Mr. McAlister is a member of Free Enterprise Dealers, Inc., which is a trade association of liquor store owners and operators scattered throughout Indiana. The Free Enterprise Dealers retain the firm I work with to represent them before the Indiana General Assembly. Our General Assembly has addressed the issue of territorial restrictions in the Malt Beverage business every year but one since 1974 and has repeatedly refused to enact such legislation.

As an individual operator and as a member of Free Enterprise Dealers, Inc., Mr. McAlister wanted me to relate to you his experiences since he has operated under both systems. Mr. McAlister presented the following statement before the Indiana State Alcoholic Beverage Commision in March of this year. The Commision was holding a hearing on the possible repeal of it's Regulation 28 which among other things prohibits the establishment of exclusive territorial distribution agreements (The Commission later voted unanimously to retain the regulation). Here is Mr. McAlister's statement:

STATEMENT IN OPPOSITION TO
THE REPEAL OF REGULATION 28 --
MARK A. McALISTER

I am Mark A. McAlister of Big Red Liquors, which operates four package store outlets in Bloomington. The effect of the Commission's proposed repeal of Regulation 28 will be to pave the way for agreements between brewers and Indiana beer wholesalers which assign exclusive territories to the wholesalers, and which limit retailers within those territories to a single source for any given brand of beer. Up until late 1973 or early 1974, this was the way that beer was distributed in Indiana. From 1974 to the present, retailers and consumers have benefitted from increasing competition between wholesalers selling the same brand. Because Big Red Liquors has operated under both systems, I believe that I am qualified to comment on the impact each has had in the market. Based upon that experience, it is absolutely clear to me that the repeal of Regulation 28 will have a disastrous effect upon beer retailers and consumers. As a result, I respectfully request that the Commission leave Regulation 28 on the books, and submit this statement in support of that position.

I. THE "GOOD OLD DAYS"

During the period that old line wholesalers undoubtedly cherish as the "golden age" of strict adherence to assigned territories, the local distributors in our market operated as follows:

(1) They took retailer orders on Monday, delivered on Monday and Tuesday afternoons, and closed early on Wednesday. They delivered on Thursday and Friday mornings, and closed early. Saturday mornings were reserved for retail keg sales to consumers.

(2) Although they now argue that exclusive territories will insure product freshness, they did not check code dates on our beer during the "good old days."

(3) Two of the three owners of local distributors never called upon us to welcome us to the market or offer assistance.

(4) Big Red Liquors did not receive any price benefit from promotional discounts routinely offered to the wholesalers by the breweries. These discounts were apparently used to pad the wholesalers' profit margins.

(5) The prices offered by the local wholesalers

on comparable packages and brands were virtually identical. If one wholesaler raised his price, the others would immediately follow, often on the same day and virtually always within the same week.

In short, the "good old days" were only good for the wholesalers.

II. THE CURRENT MARKET

We were among the first to take advantage of the emergence of price competition in the wholesale market by sending our trucks to Winamac, Indiana in order to pick up beer at the wholesalers' docks. When this "retailer hauling" was prohibited in June, 1978, we were the first to receive delivery from Beerco in Hartford City, who hauled beer to us despite the fact that we weren't in "their territory." We saved an average of $0.50 - $1.50 per case under the local wholesalers' prices.

The reaction of our local wholesalers to competition was varied. Best Beers of Bloomington, Bloomington's largest wholesaler (Anheuser-Busch, Stroh and Miller) responded in a regressive manner:

(1) They Raised prices to their other customers to offset the loss of our business;

(2) Persons believed to be employees of Best Beers smashed headlights and slashed tires on our trucks, and harassed our employees;

(3) They Have not called on us in over two years (although the new Budweiser Light brand is currently the object of an intensive promotional campaign, we have yet to be contacted);

(4) They Solicit keg sales on the Indiana University campus and have even picked up kegs on the campus; and

(5) Have sold kegs to consumers at a price below that which they sell to retailers -- thus ignoring the needs of retailers who still buy locally.

As a result of these poor decisions, their business is suffering.

Monroe Beverage (Miller Lite), on the other hand, has reacted in a progressive way to changes in the market. Because they have responded to competition, we have worked with them to make Miller Lite our best-selling brand. Our account with Monroe Beverage is up, they have hired an additional employee, our Miller Lite sales are increasing and the wholesaler has been doing a good business for the past three years. This approach makes sense.

III. THE BENEFITS OF COMPETITION

We have employed extra people whose primary responsibility is to rotate our beer. Many of the jobs being lost by old line wholesalers who don't want to compete are being picked up by progressive wholesalers and retailers. As a result of competition, we _must_ have fresh product -- we check it weekly. Likewise, our suppliers (_e.g._ Beerco, Tippecanoe Beverage, Better Brands and Monroe Beverage) check code dates monthly.

Most importantly, we are passing on our savings to our customers. During all of the debate which has occurred before the Legislature's ABC Study Committee and in connection with the various "Beer Baron Bills" of the past, I have yet to hear a consumer complain about the lower retail prices brought on by competition. None of our customers have suggested to us that we buy beer locally and raise _our_ prices in order to cover increased costs.

Likewise, even small retailers can take advantage of the savings being offered by competitive wholesalers -- many of them offer discounts on small quantities which are affordable for any retailer. Further, competition gives small retailers the opportunity to expand if they so desire. We started out as a "mom and pop" store selling a pallet of beer per week, but we were able to expand by utilizing modern business practices and taking advantage of the cost-savings offered by competition at the wholesale level. A return to the exclusive territories of the past would largely eliminate these incentives and opportunities, and the competitive retail prices which result.

V. CONCLUSION

Competition is keen between the various types of retailer permittees, all of whom are trying to provide consumers with quality products, good service and lower prices. There is utterly no reason that wholesalers should not be expected to do the same. Competition has been the key ingredient to better distribution and lower prices in Monroe County. If we go back to the days of exclusive territories, the 55,000 people in our county will be forced to bear the burdens of inefficiency and higher prices so that three wholesalers can prosper in a captive market. Competition has brought the beer industry out of the dark ages, and it must be preserved for the good of the entire industry and the citizens of this state.

For all of these reasons, Regulation 28 should remain in effect.

Mark A. McAlister
March 23, 1982

Senator SIMPSON. Mr. Quinn?

Mr. QUINN. Thank you, Mr. Chairman. My name is Richard Quinn. I have been in the beer wholesale business in Indiana since 1971. My testimony today is in behalf of the Indiana Malt Beverage Association, a trade association dedicated to the free enterprise system of selling beer at wholesale and formed specifically to assist in preventing exclusive territory legislation from being enacted in Indiana.

S. 1215 would not mandate the breweries to enter into exclusive territory agreements with each wholesaler, as did the legislation in Indiana, but would only allow such agreements to exist under the protection of law. If a brewery chose to under this proposed system, it could establish dual distributorships in certain areas and exclusive territories in others. This happened in Indianapolis in the early 1970's when the Schlitz Brewery became dissatisfied with its then exclusive distributor. Schlitz tried unsuccessfully to convince Capital City Supply Co. to sell out to Monarch Beverage. When their distributor and the chosen buyer could not come to terms, Schlitz appointed Monarch Beverage as its second Indianapolis wholesaler. This action quickly convinced Capital City to sell out. So, Schlitz had their chosen new distributor selling Schlitz products in Indianapolis to the financial detriment of its former wholesaler. The Schlitz Brewing Company created intrabrand competition in Indianapolis to serve its own ends.

To this day, Miller Brewing Company has two Miller Lite distributors in many Indiana counties. In 1972, Miller Brewing Company bought the Meisterbrau Brewery in Chicago and acquired the Lite brand. As breweries have gone out of business in the recent past, other breweries have acquired those brands and distributors and in Indiana today it is not unusual for the G. Heileman Brewing Company, for instance, to have three distributors in an Indiana county, each selling different Heileman brands.

However, Miller Brewing Co. gave most of their Miller High Life distributors the Lite brand. But where they had a Lite distributor in the same county, they did not give the Lite distributor the Miller High Life brand. This decision by Miller created enormous inequities as the Lite distributor was unable to compete with the full-line Miller distributor because Miller would not give the Lite distributor the full line. I was a Lite-only distributor in this dual situation in Anderson, Ind. In a move to attempt to compete on an equal basis with the local full-line Miller distributor, I entered into an agreement to purchase the full-line Miller distributor in an adjacent county. Although I was rated by Miller as one of the better wholesalers in the State, Miller refused to approve my purchase of this business, and I had no other choice but to sell my business to the local full-line Miller distributor.

Much has been said about fresh product and quality control. Breweries claim they can best assure the consumer fresh product if only one distributor sells each brand in a given market. To have it otherwise, they claim, means they cannot accurately hold a distributor responsible if overage product remains on a retailer's shelf. I have with me three forms designed by Miller Brewing Co., Stroh Brewing Co., and Anheuser Busch, Inc. Copies of these forms, by the way, are attached to the written portion of my remarks.

These breweries insist that we free market wholesalers complete these forms for each delivery we make outside of our assigned territory. We detail for these breweries each account we sell, the date we deliver the beer, the specific package and volume of beer and the code date on each case. We spend hundreds of manhours each month to accurately supply this information to our suppliers, and we do this at their insistance.

Distributors who ask you to enact legislation to enable breweries to protect them from intrabrand competition claim that they cannot compete with us because we have all the brands and just deliver the large volume accounts whereas they must service all accounts in their area no matter how small or costly the delivery is. Allow me to address both of these contentions.

We do have most brands in our company. Yet, we acquired most of these brands through a merger 5 years ago. We were forced to merge because free market wholesalers had begun selling to retailers in our small market. After the merger, we found that the only way we could lower our price to compete with the free market wholesalers was to expand our market. So, we sought new customers. We have invested hundreds of thousands of dollars in computers, trucks, and warehouses in order to thrive and survive in this innovative, competitive method of distributing beer.

It is interesting to note that during the Stroh Brewing Co.'s recent distributor meetings, the main thrust of their presentation to us was that they had to grow or go. They revealed the rationale for their purchase of the Joseph Schlitz Brewing Co. brands and facilities. They said that without greater geographical distribution and more brands and therefore more volume, they were doomed. These are the people who come to the U.S. Senate and ask you to allow them to stifle our growth.

My prepared remarks have statistics that show that our company and our member companies service all types of customers, all sizes of customers.

The reality of this situation, Mr. Chairman, is that you are being asked to referee an intraindustry battle. The reason that most Indiana free market wholesalers come from small towns is that they had a choice: expand their market or go out of business. Or as Stroh Brewing Co. has phrased it: grow or go. Had the giant beer wholesalers in Indiana reacted economically to our intrusion into their markets, they would have driven small companies like ours were then out of their markets and therefore out of business. But the protected, noncompetitive wholesalers went to the Indiana General Assembly and asked them to solve their economic problems while we were solving ours in the marketplace.

They were singularly unsuccessful at the State level, and so they have come to you.

Thank you.

Senator SIMPSON. Thank you very much. It is very interesting concluding testimony. Without objection, we will insert your prepared statement.

[Material referred to follows:]

TESTIMONY
OF
RICHARD M. QUINN
VICE PRESIDENT - INDIANA MALT BEVERAGE ASSOCIATION

Mr. Chairman, members of the committee, I have been in the beer wholesale business in Indiana since 1971. My testimony today is in behalf of the Indiana Malt Beverage Association, a trade association dedicated to the free enterprise system of selling beer at wholesale and formed specifically to assist in preventing exclusive territory legislation from being enacted in Indiana.

S-1215 would not mandate the breweries to enter into exclusive territory agreements with each wholesaler, as did the proposed legislation in Indiana, but would only allow such agreements to exist under the protection of law. If a brewery chose to under this proposed system, it could establish dual distributorships in certain areas and exclusive territories in others. This happened in Indianapolis in the early 1970's when the Schlitz Brewery became dissatisfied with its then exclusive distributor. Schlitz tried unsuccessfully to convince Capital City Supply Company to sell out to Monarch Beverage Company and when their distributor and the chosen buyer could not come to terms, Schlitz appointed Monarch Beverage as its second Indianapolis distributor. This action quickly convinced Capital City to sell out. So, Schlitz had their chosen new distributor selling Schlitz products in Indianapolis to the financial detriment of its former wholesaler. The Schlitz Brewing Company created intrabrand competition in Indianapolis to serve its own ends.

To this day, Miller Brewing Company has two Miller Lite distributors in many Indiana counties. In 1972, Miller Brewing Company bought the Meisterbrau Brewery in Chicago and acquired the Lite brand. As breweries have gone out of business in the recent past, other breweries have acquired those brands and distributors and in Indiana today it is not unusual for G. Heilman Brewing Company to have three distributors in an Indiana county, each selling different Heilman brands. However, Miller Brewing Company gave most of their Miller High Life distributors the Lite brand. But where they had a Lite distributor in the same county, did not give the Lite distributor the Miller High Life brand. This decision by Miller created enormous inequities as the Lite distributor was unable to compete with the full line Miller distributor because Miller would not give the Lite distributor the full line. I was a "Lite only" distributor in this dual situation in Anderson, Indiana and in a move to attempt to compete on an equal basis with the local full line Miller distributor, I entered into an agreement to purchase the full line Miller distributor in an adjacent county. Although I was rated by Miller as one of the better wholesalers in the state, Miller refused to approve my purchase of this business and I had no other choice but to sell my business to the local full line Miller distributor.

From the foregoing examples, one can conclude that breweries may be not in favor of wholesalers competing on their brands unless it serves their specific purpose; and in that case, they then have no hesitancy to create competing situations on the same brand. Intrabrand competition apparently is good only if it serves the breweries desired goals.

Much has been said about fresh product and quality control. Breweries claim they can best assure the consumer fresh product if only one distributor sells each brand in a given market. To have it otherwise, they claim, means they cannot accurately hold a distributor responsible if over age product remains on a retailers shelf. I have with me three forms, designed by Miller Brewing Company, Stroh Brewing Company and Anheuser Busch, Inc. These breweries insist that we free market wholesalers complete these forms for each delivery we make outside of our assigned territory. We detail for these breweries each account we sell, the date we deliver the beer, the specific package and volume of beer and the code date on each case. We spend hundreds of man hours each month to accurately supply this information to our suppliers and we do that at their insistance.

Our member companies constantly train retailer personnel so that they are aware of proper product rotation to insure product freshness. We have seperate crews that constantly do fresh product checks in accounts we sell and if the product does become out of date on a retailers shelf, we replace the beer and destroy the old beer at our expense. Last year, our company destroyed thousands of dollars worth of over age products - again at our expense.

Distributors who ask you to enact legislation to enable breweries to protect them from intrabrand competition claim that they cannot compete with us because we have all the brands and just deliver the large volume accounts whereas they must service all accounts in their area no matter how small or costly the delivery is. Allow me to address both of these contentions:

First - that we have all the brands and they have only one or two. Our member companies sell a brand mix that ranges from our company in Hartford City, Indiana which sells brands that enjoy 80% of the volume of beer sold in the state to Schembre Beverage Company of Kokomo which has brands representating only 15% of the beer volume in Indiana. Of the six best selling labels, Schembre has only one, Olympia, which is the sixth largest selling in the state. We acquired most brands through a merger five years ago. We were forced to merge because free market wholesalers had begun selling to retailers in our market. After the merger, we found that the only way we could lower our price to compete with free market wholesalers was to expand our market and so we sought new customers. We have invested hundreds of thousands of dollars in computers, trucks and warehouses in order to survive and thrive in this innovative, competitive method of distributing beer.

It is interesting to note that during the Stroh Brewing Company's recent distributor meetings, the main thrust of their presentation to us was that they had to "grow or go." They revealed the rationale for their purchase of the Jos. Schlitz Brewing Company brands and facilities. They said that without greater geographical distribution and more brands and therefore more volume, they were doomed. These are the people who come to the United States Senate and ask you to allow them to stifle our growth.

Let me address the charge that free market distributors only sell volume accounts. The following is a delivery volume breakdown for the last week in May for Schembre Beverage of Kokomo.

Number of Cases	% of Total Deliveries
1 - 25	42%
26 - 75	29%
76 - 200	20%
200+	10%

During that same week, our company's delivery profile was:

Number of Cases	% of Total Deliveries
1 - 100	35%
101 - 500	15%
501 - 1500	17%
1500+	33%
	100%

The free market method of selling beer does inhibit wholesalers from investing their own dollars in advertising and promotion because another wholesaler may benefit from it. In 1975, I was told by a Miller Brewing Company official that advertising was the brewery's responsibility and was informed that the brewery would create the consumer demand and our job was to establish and maintain maximum distribution to fill that demand.

The practical reality is that it is more efficient to coordinate advertising effort from the brewery and if a brewery wants distributors to participate in the cost of the advertising effort, all it has to do is add a few cents per case to the cost of our beer.

Gentlemen, the reality of this situation is that you are being asked to referee an intra industry battle. The reason most Indiana free market wholesalers come from small towns is that they had a choice, expand their market or go out of business! Or as Stroh Brewing Company has phrased it: "Grow or go." Had the giant beer wholesalers reacted economically to our intrusion into their markets, they would have driven small companies like ours were then out of their markets and therefore out of business. But the protected, non-competitive wholesalers went to the Indiana General Assembly and asked them to solve their economic problems while we were solving ours in the marketplace.

They were singularly unsuccessful at the state level, and so they have come to you.

Thank you.

Miller

OUT OF COUNTY SALES MONTHLY REPORT

For month of ____________ Date: ________________

Retail Account Name: ______________ D/B/A/ ________

Address: ____________________ City: ____________

Date of Sale	Package Description	No. of Cases Sold

Stroh

TRANSACTION DATA SHEET

WHOLESALER ______

COUNTY ______

ACCOUNT NAME ______

STREET ADDRESS & CITY ______

DELIVERY DATE ______

QUANTITY	PACKAGE	CODE DATE	QUANTITY	PACKAGE	CODE DATE

COUNTY ______

ACCOUNT NAME ______

STREET ADDRESS & CITY ______

DELIVERY DATE ______

QUANTITY	PACKAGE	CODE DATE	QUANTITY	PACKAGE	CODE DATE

Cols.1-5 51333 Whslr ID

6 - 9 Mo/Yr.

ANHEUSER-BUSCH INDIANA WHOLESALER

OUT-OF-COUNTY SALES FORM

FORM A

DATE ________

10-14	15-19	20-21	22-24	25-27	28-29	30-32	33-35	36-37	38-40	41-43	44-45	46-48	49-51	52-53	54-56	57-59	60-61	62-64	65-67
Retailer ID	Prod/CTN Code	Day	QTY	Code	Day	QTY	Code	Day	QTY	Code	Day	QTY	Code	Day	QTY	Code	Day	QTY	Code

Senator SIMPSON. I must say if the things I think you say, Mr. Lackey, were true throughout the wholesale industry and truly typical, there could not be many successful wholesalers operating. And I am sure that those that you indicate are not maybe a continual picture but just simply isolated or your testimony, too. I do not know. Anyway, I cannot imagine how anyone can stay in business very long as a wholesaler and engage in that kind of activity somehow.

Let me ask you this question. In the previous panel Mr. Pohl gave us figures that indicate the situation in Indiana has grown less favorable for the small brewer. That is what you were discussing there. He thought that was because Indiana's nonexclusivity makes this transshipping more attractive for national instead of for local brands. You indicate that you were going to comment on that, but you did not. If you would please, because I think that is a very important issue that has obviously been discussed more than several times today. Do you have a comment on that?

Mr. QUINN. I was not involved with this company at the time, but as I understand it when our company began transshipping, the Hudepohl Brewing Co. stopped selling us beer. We had the Hudepohl brand at one time but no longer have it. So, our company does not sell that brand even though we are the largest wholesaler in the State. We do not sell that brand at the pleasure of the Hudepohl Brewing Co.

Senator SIMPSON. No, I do not think he was talking about simply one; he was talking about all of the smaller ones.

Mr. QUINN. The smaller brewing companies are losing market share. There is no doubt about that at all nationally. In certain areas small brewing companies such as Hudepohl or one or two others in Ohio that are doing very well, and we are doing very well by them also when we sell their brands. We do not just sell the national labels if that is the contention.

Mr. LACKEY. Mr. Chairman, if I could interject here, I do not think that the condition of the small brewery really has anything to do with this particular issue, especially in Indiana. Our stores buy based on what our customers want. In other words, the customer demands and determines what is going to be on our shelves. Basically, I think what is happening is that the large breweries are doing a much better job of advertising and campaigning on a national level and are creating some of the demand and taking it away from some of the smaller breweries.

It is important to note, too, that Falstaff also has come out in opposition to this bill.

Senator SIMPSON. Let me ask you this, Mr. Lackey. Proponents of S. 1215 argue that interbrand competition is very fierce in the malt beverage industry and that this would prevent the type of situations that were common in Indiana prior to 1974. Would you comment on that please?

Mr. LACKEY. Yes, sir. And responding to your earlier comments the reason those situations existed was because the retailer had absolutely no alternative. He had nowhere else he could go to buy. He either got out of the business or he took it at the price and under the conditions that the local wholesaler dictated. And it got way out of hand. It got to those types of conditions. Those were not exceptional. Not only to grocers, but the same was true of liquor stores, taverns, and restaurants.

Senator SIMPSON. Let us say that this issue of transshipment has been apparent in the industry in the past. Do you know whether the incidence of transshipment increased greatly in Indiana since the law was changed to prohibit exclusive territories?

Mr. LACKEY. In my written remarks, Mr. Chairman, I tried to cover that. It is a very good question. The majority of beer being sold in Indiana is not being sold by transshippers. It is being sold locally. The difference is that because of the transshipper alternative now the local wholesaler is much more responsive to the needs of the retailer. I have had many of my grocers say I am buying locally, but I am buying locally only because the transshipper gives me the option and consequently makes the local wholesaler competitive. He is selling at a more competitive price. He is responsive. He fills special orders. He insures quality is taken care of much more so than we ever had before.

Senator SIMPSON. If it can be proven that there is, quote, "substantial and effective competition" unquote, between brands in a given territory, as is a specific requirement and the language of S. 1215, substantial and effective competition before an exclusive territorial arrangement can be approved, would not that insure that the retailers and consumers would be protected from increased prices and reduced service from distributors?

Mr. LACKEY. No, sir, not necessarily. Basically, you would have the brewery in a position to control the prices directly to the retail level. They would fluctuate prices in an attempt to obtain a particular share of market and for a short period of time they would increase the prices. Then, once they obtained that share of market that they were trying to achieve, they would go back to the much higher price rate.

I think Dick can comment on this, too. We saw this happen repeatedly in Indiana when the beer baron was in place.

Senator SIMPSON. Well, of course, S. 1215 would not change the system which would allow any other State if it wished to prohibit exclusive distributorships as Indiana has done. But I would believe–and it will be interesting to review the testimony completely and the questions of my colleagues—that still the inattention or callousness on the part of a wholesaler, even an exclusive distributor, could easily, I think, impinge upon his business or at least cut into his profits by driving customers to other brands. And that will always be the case. You would admit that, would you not?

Mr. SIMMONS. No, sir.

Mr. LACKEY. The customer is the ultimate decisionmaker about what brands are going to sell.

Senator SIMPSON. Well, you have given us some provocative material, and that is what we were after in the hearing process. I am very appreciative to all of you who have testified. It has been very helpful. We will give the committee a good deal of information to process. I thank you very much, all of you.

The record will be held open for 2 weeks for entry of further information.

Thank you very much. This will conclude the hearing today on S. 1215.

[Whereupon, at 12:50 p.m., the hearing was adjourned.]

[The following was subsequently supplied for the record:]

Suite 760, 101 East Ontario Street, Chicago, Illinois 60611 • (312) 951-8878
Russell G. Hopkins

National Wine Distributors Association

May 26, 1982

Honorable Strom Thurmond, Chairman
Senate Judiciary Committee
Washington, D.C. 20510

Dear Senator Thurmond:

The Malt Beverage Interbrand Competition Act seeks to confirm the legitimacy of territorial restrictions employed in the brewing industry.

In order to procure wholesaler partners and encourage them to vigorously promote their brands, brewers have utilized various forms of exclusive territorial arrangements over the years.

No one can deny that the exclusive territorial system has been accompanied by substantial competition. An examination of consumer price indexes and sales concentration ratios will confirm the existence of such competition.

Moreover, exclusive territorial arrangements of one type or another are by no means unique to the brewing or softdrink industries - the exclusivity feature is critical to the field of franchising itself which has instilled a great deal of competition into virtually every sector of our economy in recent decades.

Therefore, the National Wine Distributors Association heartily endorses the principle underlying S. 1215 that exclusive territorial arrangements that are pro-competitive be acknowledged as permissible under the antitrust laws.

While we have no objection to the softdrink and beer industries being granted limited immunity from the antitrust laws, we ask the Judiciary Committee to give serious consideration to extending the same privilege to all other branches of the franchising field as well.

Respectfully submitted,
Russell G. Hopkins
Russell G. Hopkins
President

RGH:jpb

Voice of the Independent Wine Distributor

INTERNATIONAL BROTHERHOOD OF TEAMSTERS
CHAUFFEURS • WAREHOUSEMEN & HELPERS
OF AMERICA
25 LOUISIANA AVENUE, N.W. • WASHINGTON, D.C. 20001

OFFICE OF
• ROY L. WILLIAMS •
GENERAL PRESIDENT

JUL 0 1 1982

June 28, 1982

The Honorable Strom Thurmond, Chairman
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Chairman Thurmond:

On behalf of an organization representing nearly two million members, we urge your active support of S.1215, the proposed Malt Beverage Interbrand Competition Act.

Background

We are the largest union in the beer industry, representing some 78,000 workers in both the production and distribution of this product. We have represented these workers since the repeal of Prohibition in 1933.

While this bill does not have a direct impact on our members employed in production of beer, it has a tremendous bearing on our 20,000 members who work in the beer distribution industry.

Most of the employers in beer wholesaling are small businesses. That is, the U.S. Department of Commerce reports that as of 1979 only 71 beer wholesalers employed more than 100 workers. Also, well over 60 percent of those employed work for establishments with fewer than 50 employees.

Saving our members' jobs is of primary importance. These workers are productive and respected members of their communities.

These jobs are now in jeopardy. We have lost over 1,500 members since 1980; and unless legislation is enacted, we will lose more jobs.

What is the cause of this?

In a word, transshipping.

Under traditional practices, beer wholesalers have sold their product within fairly well defined geographic territories, thereby providing stable service for all customers within a particular area.

However, in recent years, some distributors have been selling outside traditional boundaries and many of these sales are made to large customers who are able, through large warehouse facilities and mass retail outlets, to take advantage of volume deliveries.

With transshipping, we are witnessing the destruction of the historical arrangement of territorial or geographical areas in which the distribution of a manufacturer's brand is assigned to a franchised or designated distributor. This system has been in effect for nearly 50 years.

That is, the marketplace has become a shambles. Transshippers travel many miles, often across state boundaries, to dump beer at non-competitive prices in a territory being served by an authorized distributor.

There are some who would say that these practices benefit consumers. We believe this is inaccurate. The so-called savings are often the result of the evasion of payment of state and local taxes. Also, transshippers care little for the quality of the products they deliver. Moreover, those consumers whose retailers can not afford transshipping will, ultimately have to pay more for the product. Finally, in jurisdictions where deposit systems are in effect, transshippers will ignore their obligation to pick up empty bottles, thus increasing the price of beer.

A wholesaler who loses sales to transshipping, particularly beer wholesalers, can not hope to stay in business. By the same measure, our members can not hope to keep their jobs if employers are losing this revenue.

In our view, the only realistic solution to this problem is the enactment of S.1215 because it will: (1) provide reasonable market certainty for beer wholesalers; and (2) protect beer distribution from being captured by large businesses, and it will maintain the vigorous competition among the various brands of beer.

1. Reasonable Market Certainty

Under existing Federal law, there is a question as to whether a brewer and a wholesale distributor can enter into a contract providing an exclusive sales territory for the wholesaler. If S.1215 is approved, the uncertainty would diminish; and wholesalers could continue to sell their products without the fear of transshipping.

That is, this bill would provide existing small businesses with a known territory in which they would compete with other wholesalers. Most of the existing wholsesalers would be able to survive in such an atmosphere, again providing job certainty for our members.

In addition, it would continue to be an efficient means for states to collect taxes on beer sold to their jurisdictions.

In 1980, over $1 billion was collected by the states from taxes imposed on beer. Most of these revenues were collected from established wholesalers. In our view, the certainty of collection was - and is - enhanced because the wholesalers are easily identifialbe and the tax system functions smoothly with wholesaler participation.

On the other hand, transshipping does not offer this degree of certainty because it is virtually impossible to identify the beer sold through this means of distribution. We agree there are other systems, like stamping, which can be used for authenticating beer sales; but we do not believe they are as efficient as collecting taxes through wholesalers.

In that regard, we have been told that nearly half of the beer sold in New York and Boston Metropolitan areas escape state and local taxation.

2. Protection for Small Businesses

In the beer industry, the seller - or brewers - are a few large companies and they are responsible for the largest share of the market.

That is, for 1981, the five largest breweries accounted for nearly 75 percent of the beer made in the United States.

In the retail buyer's section of the market, food stores in 1979 accounted for 64 percent of the beer sales.

Again, the retail food industry shows a fairly high degree of concentration. In 1981, chain supermarkets, which represented only 11 percent of all grocery stores in the country, accounted for nearly 50 percent of all grocery store sales.

In the middle, of course, are the beer wholesalers - small businesses.

Given the dimensions of these wholesalers' sellers and buyers, it is apparent to us that, without some protection, these wholesalers will be put out of business.

What we see is the following: wholesalers will continue to lose large volume accounts to transshipping and, eventually, go out of business.

A number of transshippers will become large point-to-point distributors of beer -- that is from the point of manufacture to the point of sale to the large volume buyer.

However, we believe the brewers will, ultimately, become dissatisfied with such a system, and they will build and operate their own distribution facilities.

And the wholesalers, as we know them, will cease to exist, along with our jobs. We do not believe this is necessary, nor do we believe the destruction of this industry will serve a public interest.

It is for this reason that we are urging the adoption of S.1215 because it will permit, under Federal law, the wholesalers and brewers to enter into territorial agreements that will save these employers.

In sum, we urge the Committee to adopt S.1215, the proposed Malt Beverage Interbrand Competition Act because it will provide reasonable market certainty for beer wholesalers and at the same time preserve a number of small businesses in our economy.

Most importantly, it will save our jobs in this industry.

Thank you for your consideration in this matter, and we would ask that this statement be made a part of the record of these proceedings.

Sincerely,

Roy L. Williams

Roy L. Williams
General President

RLW:bb

FOOD MARKETING INSTITUTE

1750 K STREET N.W.
WASHINGTON, D.C. 20006

TELEPHONE (202) 452-8444
TELEX 892722 FMI USA WSH

July 12, 1982

The Honorable Strom Thurmond
Committee Chairman on the Judiciary
U.S. Senate
Washington, D.C. 20510

Dear Mr. Chairman:

We are submitting for the record our response to the questions you posed to Frederik Meijer, Food Marketing Institute's Vice Chairman, subsequent to his appearance before the Committee in opposition to S. 1215.

Question No. (1)

When you make the statement that this bill will remove any incentive on the part of the distributor to be responsive to his retail customers, aren't you overlooking the fact that competition from other brands must be considered and dealt with by that distributor?

Answer

No, it is not overlooked. Brewers spend substantial sums (Anheuser-Busch spent $181 million in 1980, Jos. Schlitz spent $66.4 million in the same year) to promote their products and they are quite successful in creating consumer demand for particular brands. A consumer who doesn't find his favorite brand on a retailer's shelf, will go across the street to a competitor the next time he needs beer. The fact that another brand is on the shelf (so-called interbrand competition) is not relevant. Retailers simply must carry those brands their customers want or they will lose their customers.

Exclusive territories mean the one designated distributor for the brand has a monopoly in that territory. Those retailers such as myself who operate where exclusive territories already exist know for a fact that service suffers and prices are higher than they would be if distributors were competing to get their brands into the stores. This is true even though interbrand competition may exist. Experience teaches that distributors

Cont'd

in these circumstances are less responsive because they know that the retailer (who is competing for customers) must carry the brand and has no choice but to turn to the designated monopolist for that brand.

Question No. (2)

Proponents of S. 1215 argue that unless this bill is passed, small retailers will be hurt by the increasing practice of "transhipping" to large retail customers which will force the local distributors out of business. Do you see this as a possibility and if so, how could it be avoided without passage of S. 1215?

Answer

No, it is not a possibility. "Transhipping" is just a term that is used to avoid saying "new competition". How can retailers of any size be harmed by having new suppliers competing for their business? It is, in fact, the smaller retailer who suffers most from a system of exclusive territories. That is because the small retailer has less leverage with the designated monopolist than his larger competition. The monopolist is therefore often more responsive to his larger customers, leaving the small retailer with absolutely no choice when he receives poor service, or even no service at all.

Wholesalers who are afraid of new competition do argue, in their own self-interest, that such competition somehow or other harms small retailers. It is not the retailers themselves who make this argument. Independent retailers are able to obtain an ample supply of all the other products sold in grocery stores without difficulty. As a result they compete quite effectively with their larger competitors. Exclusive territories are not necessary to insure the supply of these products and likewise they are not needed to insure the supply of beer.

If brewers and wholesalers are concerned about service to small retailers they need only enforce distribution agreements which, I understand, require distributors to meet minimum service standards.

Sincerely,

George R. Green
Counsel

GRG/cl

Mr. Seymour Podolsky
Beverage Distributing Co.
19000 Northline Road
Southgate, Michigan 48195

July 20, 1982

Senator Strom Thurmond
Chairman,Senate Judiciary Committee
2226 Dirksen Senate Office Building
Washington, D.C. 20510

Dear Mr. Chairman:

Thank you very much for providing me with the opportunity to give you additional information on S.1215 per the six questions attached to your letter of July 2nd. For the sake of clarity, I have taken the liberty of repeating your questions prior to each of my answers.

1) "DOESN'T THE 21st AMENDMENT APPLY EQUALLY TO WINE AND DISTILLED SPIRITS AS WELL AS TO MALT BEVERAGES, SO THAT IF WE ACCEPT THE NEED FOR LEGISLATION IN THIS CASE, THESE OTHER INDUSTRIES WILL RIGHTFULLY BE THE NEXT IN LINE?"

We are in full agreement that the 21st Amendment applies to the entire alcohol beverage industry. We are not thoroughly apprised of the nuances of the distribution problems related to the wine and distilled spirits industries. We do not know if their needs are as pressing as those of the beer distributors. We do know, for example, that while beer is a perishable product, many wines actually improve with age as do some distilled spirits. We also know that our product must be kept refrigerated where theirs do not and the sheer volume of our business requires our basic measure to be in millions of barrels vs. millions of gallons for the other spirits. We feel that the protection of S.1215 is essential for our portion of the industry and assume that similar protection would be helpful to those other industries but we are unable to comment on its crucial nature.

2) "IN THOSE STATES WHICH DO NOT HAVE LEGISLATION PERMITTING EXCLUSIVE TERRITORIES, WON'T PASSAGE OF S.1215 ALTER THE STATUS QUO AND FORCE STATES TO ACT IF THEY WANT TO PRESERVE THE MARKETING SYSTEM PRESENTLY IN EFFECT?"

The passage of S.1215 will not affect any state law nor will it affect or alter the status quo in any state not having territorial legislation . As indicated in our original brief, 25 states currently have statutes either mandating or permitting exclulusive territories specifically. Another 13 states have statutes which imply exclusive territories (i.e. prohibiting dual distributors in any territory.) 12 states have no statute on the subject and Indiana has a beverage commission regulation prohibiting exclusive territories. The law in the 12 states that are currently statutorily silent is that of the GTE Sylvania decision of the Supreme Court which provides that vertical non-price restrictions in restrictions in interbrand competition by a brand owner to foster interbrand competition are not per se illegal but, rather, must be judged under the "rule of reason."

The passage of S.1215 will have only one small limited effect in these 49 states plus the District of Columbia. It would remove the challenge to any of the 38 state statutes plus the Sylvania arrangements in the other 12 on "rule of reason" grounds. It has been the tactic of the huge retail marketing chains to use "rule of reason" challenges to state statutes or contractual arrangement in the hope of eliminating distributors and, eventually, retail competitors. While we have been generally successful in defending these suits, we cannot continue to afford legal fees running well over a quarter of a million dollars that are hardly felt by the chain retailers. It is our opinion that this issue was raised by the chain retailers with the hope of convincing the committee to maintain the status quo so that they can continue their war of attrition. We can assure you that the passage of S.1215 will do absolutely nothing to the status of the law or marketing system in any state. It merely removes the "rule of reason" challenge and makes exclusive territories per se legal when they meet the significant interbrand competition test."

3) "EXCLUSIVE TERRITORIES MEAN THERE IS ONLY ONE WHOLESALER FROM WHOM RETAILERS CAN PURCHASE. WHAT CAN A GROCER OR TAVERN OWNER DO IF HE RECEIVES BAD SERVICE OR HIGH PRICES FROM HIS WHOLESALER?"

The retailer has a multitude of remedies available to him concerning any complaint he may have about his wholesale supplier. Every state in the United States has some form of law or regulation dealing with malt beverage price discrimination. Furthermore, every state licenses its wholesalers in addition to the federal permit that is required. The state license provides specific complaint and review procedures for retailer complaints. We would further like to point out clauses permitting the brewer to cancel the agreement if the wholesaler does not provide the highest level of service in keeping with the company's national image and the movement of products at competitive prices to try and maintain an effective investment in service, image, quality, good-will, and market share. Competition in the beer business is extremely vigorous and has been for many years. Beer has remained the second lowest product on the consumer price index for the last 40 years. During this period of time, many wholesalers have had their supply contracts terminated for poor retailer service with a resultant loss of a very substantial investment (current average exceeds $3 million) in their distributorship. We can guarantee to you that, if state regulationslations alone did not adequately protect the retailer, the threatned loss of a franchise is more than enough incentive for good service.

4) "HOW BIG A PROBLEM IS TRANSSHIPPING IN THE INDUSTRY TODAY?"

Transshipping is a serious problem in our industry today in two respects. Before discussing these, let me generally define how it works. In states which do not have exclusive territories and where no private vertical arrangements are in effect, wholesalers are assigned what is known as an "area of primary responsibility." Under the franchise agreement, the wholesaler is responsible for his supplier's products in that area. He must constantly rotate the stock and remove-at his own expense-all beer that is past the sell date (stale beer). He must also engage in company image programs (i.e. rmoove damaged cans, torn packages, washing trucks every day, etc.) as well as engaging in expensive advertising and promotion activities. Within the territory, a wholesaler must serve every class of customer from a five-case drop at a small "mom and pop" store to truckload lots to superarkets and chain liquor stores. He will provide draft beer in quantities from two or three kegs at a small restaurant to upwards of 100 kegs at large tap outlets such as sports stadia, beer halls, etc. In addition to this, the wholesaler also services all of the tap equipment and provides advertising signs and other paraphenalia as permitted by local law.

The tactic of the transshipper is to go outside his area of responsibility and solicit only the large-volume accounts for either truckload or half truckload lots. Since this is extraordinary business for the transshipper, he offers the product at anywhere from 20 cents to 50 cents a case above his cost. He then hires a contract hauler to pick up the beer from the brewer and deliver it in one drop directly to the chain retailer. This price is already below that which the local wholesaler in that market can afford to sell the beer and pay for all of the services otherwise required of him in his "area of primary responsibility."

As we stated earlier, this situation creates two major problems. First, the companies who engage in transshipping are generally from very small towns where there are few, if any, major chain retailers located. This, of coursee, makes them immune from retaliation by the wholesalers into whose areas he is transshipping. Secondly, becuase the transshippers are generally located in small towns, they tend to have most of the brands of beer that are available. The wholesaler whose territory he is raiding or "cherry-picking" does not have this luxury. In major markets, most wholesalers tend to have a single source of supply, i.e., Miller, Schlitz, Pabst, etc. As the transshipper begins to take away the major volume accounts from another wholesaler's "area of responsibility" that wholesaler has no other products to fall back on. The loss of his volume business will cause him to restructure his operations and cut service in an attempt to be price competitive. In most cases, that has been unsuccessful and has caused them to have to raise their prices to other smaller accounts becuase the distribution cost was no longer being supported by large volume dropoffs. This creates an additional price disparity between the large and small retailers and has resulted in the demise of many samall retailers. It has also resulted in the demise of many wholesalers, most of whom were large prosperous business in major metropolitan areas. This practice is rampant in Indiana where there is regulation prohibiting exclusive territories. Testimony presented by Beerco, Inc. of Hartford City, Indiana would lead you to believe that this practice was in the consumer's best interest. Mr. Richard Quinn, testifying for Beerco, indicated that they serve every class of customer from Beerco's warehouse. Yet on the public record of the U.S. House of Representatives Committeee hearing, he publicly stated that they served all customers only in their "area of primary responsibility." Beerco is a classic case of the transshipper. They are the only wholesaler in Hartford City and they carry every brand of beer. They now offer those brands statewide in truck-load lots. Mr. Quinn has classified this as a new form of competition but the question remains -- at whose expense?

The demise of the local wholesalers who are directly responsible to the state and local community results in chaos in the marketplace. It mases it difficult for the state and local commmunities to control tax collections, recycling and recovery of litter, advertising promotions, etc. Yet this very experience is being used by these profiteering chain retailers as "rule of reason" grounds for challenging the laws and regulations of the 38 states that prohibit this practice. While we cannot state that transshipping is a serious problem all over the U.S., it has become very serious in New York, New Jersey, Massachusetts and Indiana. In the metropolitan New York City area it now even transcends state lines. Its continued growth provides us with the need for enactment of S.1215.

5) "HOW MUCH ADVERTISING AND PROMOTION DO WHOLESALERS PERFORM?

While there is no set amount that each wholesaler must provide in advertising and promotion, each is required by his franchise agreement to engage in point of purchase and local advertising sales and special promotional events. My own company handles the products of the Stroh Brewing Company and spends an average of 31.7 cents per case in direct local promotional cost. This amounts to about $158,000 per year. I am informed the Anheuser-Busch and Miller wholesalers generally spend about 41.5 cents per case and we believe that this is closer to the average for the entire 3500 distributors nationwide. In addition, we would like to point out that most of the promotional events which wholesalers sponsor are run in conjunction with local charity and all proceeds go to the charity. It is estimated by the NationalBeer Wholesalers' Association that upwards of $10 million is raised annually in these events.

6) a."HOW MUCH LITIGATION INVOLVES THE BEER INDUSTRY?"

As of this date, we are unable to give you a definite number of pending court cases in the beer industry on this issue. We are, however, able to pinpoint cases in California, New York, Kentucky, New Mexico, Illinois, Wisconsin, South Dakota and Indiana. The Indiana case is enlightening in that one plaintiff has been able to tie up the entire beer distribution network in what is now clearly an unwarranted litigation (see document enclosled).[1] This case has dragged through the courts for several years and caused the defendant beer distributors in excess of $300,000 in legal fees and the judge has just indicated he will dismiss the complaint unless the plaintiff can show further cause why it should be continued. It is this very thing and the resultant cost which must be passed on to the consumer that S.1215 is intended to prevent.

b."SHOULDN'T IT BE COMPLETELY CLEAR THAT THERE WILL BE NO ANTICOMPETATIVE RESULTS BEFORE AN ANTITRUST EXEMPTION IS LEGISLATIVELY MANDATED?"

We are in complete agreement that it should be clear there will be no anticompetitive results from this legislation. We believe that our original statement, together with the answers above, make it very clear that the passage of S.1215 will not result in any anticompetitive situations. It would do no more than remove a legal tool being employed by chain retailers to try and destroy a well-balanced highly competitive distribution system in order to increase their economic domination of the market. We further believe that, by addition of the "significant interbrand competition" requirements contained in the proposed legislation, we have actually added an additional competitive protection for the consumer that does not now exist under current antitrust protection.

We thank you for providing us with this opportunity to be of further help in your deliberating process. We again urge you to act with all due haste to bring this bill to the floor of the Senate before irreparable damage is caused unnecessarily to a well-functioning system of malt beverage distribution. Sixty-seven of your colleagues have officially co-sponsored this legislation and we hope, in the interest of the people that they represent, they will have an early opportunity to vote on its merits.

As always, we stand ready to provide you any additional information you may require.

Sincerely,

Seymour Podolsky/se

Seymour Podolsky

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[1] Document has been placed in Committee files.

P.O. BOX 350
LATROBE, PENNSYLVANIA 15650

Rolling Rock
Premium Beer

Latrobe Brewing Company

August 17, 1982

The Honorable Strom Thurmond
United States Senate
Committee on the Judiciary
Washington, D.C. 20510

Dear Senator Thurmond:

An interesting fact that you should note about your letter of July 2, 1982 addressed to me was that it was delayed by having been lost on the floor of one of the taxi cabs in Washington, D.C. Fortunately, the letter was found by some very honest people from Rockwell International who then proceeded to pick up an envelope which had a little foot wear and tear, search out the address, place a call to me and eventually put it in an envelope and pay postage and mail it on to Latrobe. This will explain the delay in our answering your question that you posed to us.

You have asked us: "What recourse does the brewer have if a wholesaler does not give service to smaller accounts?" Additionally, you requested how often this situation has occurred in our experience.

In answering the first part, "What recourse does the brewer have if a wholesaler does not give good service to smaller accounts?" We must discuss both the association between the brewer and the wholesaler and the wholesaler's protections given to him or afforded to him by various state regulations that are in existence today. Our association with our wholesalers has been that we expect them to service every licensee within the geographic area that we have agreed with them that they will service. It is their responsibility to stay current as to who the licensees are, how many there are, and of what type they may be. Much of this information comes from state, county or local information which generally controls the licensing in areas. Our understanding with our wholesalers is that they are responsible for each account regardless of size. If we find that a wholesaler is not giving service either to smaller accounts or possibly to those accounts within his geographic area that become marginally profitable due to distance of travel or other time demands, we must then take additional time to sit down with these

"Brewed From Mountain Spring Water"

individuals to review the area as a problem and to request that they begin servicing these areas immediately. In some instances we have found that geographic selections among wholesalers are not proper due to their travel patterns. When problems such as this are discovered, we will normally sit down and review with the wholesaler in question and also with surrounding wholesalers to determine if there is a better and more equitable way for them to expend their time, their efforts and their sales energies to do a better job for themselves and for Latrobe Brewing Company.

The second part of your question as to how often the situation has occurred where the wholesaler does not give service to smaller accounts we can also address. Over the years the Latrobe Brewing Company has been in business we have had very few, if any, problems with our wholesalers in any market areas. Occasionally when there is a change in ownership or a change in transfer of ownership from one generation to another or when some of the other competing beers which our wholesalers do handle become more or less active, we will find the potential of some accounts being missed. The normal trade reference would be high spotting or addressing only those accounts which are volume purchasers. If we were to make an honest appraisal of the number of times it has occurred, we could probably say that in our association with 200 wholesale areas, we could probably count on one hand the number of problems we have had over the years. The problems that we are experiencing today are now bordering on this area since the time demands of some larger brewers upon wholesalers with whom we're also associated can potentially exclude us from normal day to day competition. There is no legislation that can cover this, and we ask for none. It is our responsibility to stay current with our market place, to be monitoring the operations of retailers, to be viewing the association of retailers with wholesalers, and to keep ourselves in current, constant, day to day touch with our wholesalers so that they understand what we want, and we are knowledgeable of how they desire to approach the problems and to stay competitive with the sale of our Rolling Rock Premium Beer.

We thank you for the opportunity to expand upon our comments and hope that this is information which will be of value to you and your Committee in its decision making.

Sincerely yours,

LATROBE BREWING COMPANY

James L. Tito

James L. Tito
Vice President

JLT/amb

MALT BEVERAGE INTERBRAND COMPETITION ACT

THURSDAY, AUGUST 5, 1982

U.S. Senate,
Committee on the Judiciary,
Washington, D.C.

The committee met, pursuant to notice, at 10:02 a.m., in room 2228, Dirksen Senate Office Building, Senator Strom Thurmond (chairman of the committee) presiding.

Present: Senators Thurmond, Simpson, and Specter.

Staff present: Marcy Tiffany, chief economist and antitrust counsel; Steve Cannon, chief antitrust counsel; Bruce Cohen and Mary Louise Westmoreland, Senator Specter's staff; Boyd Hollingsworth, Senator Simpson's staff; Debbie Freshwater, Senator East's staff; Arthur Briskman, Senator Heflin's staff; and Juanita Donaghey, Senator Denton's staff.

The Chairman. The committee will come to order.

The hearing today is on S. 1215, the Malt Beverage Interbrand Competition Act. Senator Grassley requested that his opening statement be placed in the record.

[Prepared statement follows:]

Prepared Statement of Senator Charles E. Grassley

Mr. Chairman, as a cosponsor of S. 1215, the Malt Beverage Interbrand Competition Act, I am pleased that the Judiciary Committee is holding hearings on this important piece of legislation.

The bill provides that nothing in the federal antitrust laws shall prevent brewers and wholesalers from entering into written agreements granting the wholesaler an exclusive right to sell a particular brand of malt beverage within a particular territory, provided that those beverages are in substantial and effective competition with other malt beverages in the same area.

Under current case law, vertical nonprice arrangements are not per se violation of the antitrust laws. Instead, the legality of these arrangements is governed by the rule of reason as enunciated in *Continental T.V., Inc.* v. *GTE Sylvania, Inc.*, 433 U.S. 36 (1977).

As the Department of Justice indicated in its April 13 letter to the House Judiciary Committee vertical nonprice arrangements can have beneficial economic effects. They can improve quality and reputation thereby allowing the public access to an improved product. The Department went on to state that these arrangements are unlawful only when they substantially weaken interbrand competition. In that section 2 of the bill states that these arrangements will be lawful so long as the product involved is in substantial and effective competition with other products within the designated geographic area, in my view this legislation is merely a codification of current malt beverage industry practice, Department of Justice Policy, and antitrust case law. If there is an indication that these agreements substantially lessen competition in a given area, it is clear that a lawsuit alleging antitrust violations may be brought. Therefore, I believe that the fear that the malt beverage industry would be immune from liability under the antitrust laws. through enactment of this legislation, is essentially unfounded.

In light of the decision in *Rice* v. *Norman Williams Co.* No. 80-1012 (1982), interpreting a California state law regulating the importation of distilled spirits into California, I believe Congressional clarification of the law is still necessary. While the United States Supreme Court has reversed this decision, the responsibility for policy making in this area properly belongs to Congress. Regulation of alcoholic beverages has been traditionally held at the state level. The passage of this legislation will ensure it remains at that level while providing reasonable protection and competition in the malt beverage industry.

The CHAIRMAN. Our first witness is Mr. Walter T. Winslow, Deputy Director, Bureau of Competition, Federal Trade Commission, Washington, D.C.

Mr. Winslow, are you ready,to proceed?

Mr. WINSLOW. I am, Mr. Chairman.

The CHAIRMAN. All right, you may proceed.

STATEMENT OF WALTER T. WINSLOW, DEPUTY DIRECTOR, BUREAU OF COMPETITION, FEDERAL TRADE COMMISSION, WASHINGTON, D.C.

Mr. WINSLOW. Mr. Chairman, I would like to thank you for this opportunity to present the views of the Federal Trade Commission concerning S. 1215, the Malt Beverage Interbrand Competition Act.

Attached to this statement is a copy of the Commission's June 11 letters to you and to Congressman Rodino, setting forth in detail the Commission's opposition to this bill. I respectfully request that the Commission's letters be included in the committee's record, as well as the Commission's prepared statement.

The CHAIRMAN. Without objection, they will be placed in the record following your oral testimony.

Mr. WINSLOW. What I will try to do today is summarize the Commission's statement, and then I will be pleased to answer any questions.

The CHAIRMAN. Now, you would like to place your whole statement in the record, I guess?

Mr. WINSLOW. I would like to put the whole statement in the record and would then like to summarize it.

The CHAIRMAN. Maybe if you could just highlight it.

Mr. WINSLOW. Yes.

The bill, S. 1215, would legalize what are known as "airtight" exclusive territorial agreements entered into between brewers and wholesalers in the malt beverage industry, provided there is substantial and effective interbrand competition.

Four points seem to the Commission to be especially relevant to the committee's consideration of this bill.

One, Congress should require proof of the unworkability of competition as a prerequisite to enacting special antitrust exemptions.

Two, the Commission is unaware of any evidence relating to the malt beveraqe industry to the showing that competition is unworkable in that industry, and in fact, one of the principal reasons cited by supporters of S. 1215 has vanished as a result of the Supreme Court's recent decision in *Rice* v. *Norman Williams Company.*

Three, procompetitive vertical territorial restraints are already legal under the Supreme Court's ruling in *GTE Sylvania,* and S.

1215 therefore could only insulate conduct which is anticompetitive and currently illegal.

Four, because of existing governmental barriers to entry in the malt beverage industry, S. 1215 might seriously reduce the opportunity for market forces to respond quickly to anticompetitive problems in the malt beverage industry. I will expand briefly on those four points.

First, it is important to recognize that the Supreme Court has called the antitrust laws "the Magna Carta of free enterprise", and as the Commission's letter indicates, "the antitrust laws reflect the Nation's fundamental policy in favor of free enterprise and competition." The National Commission for the Review of Antitrust Laws and Procedures recommended that antitrust exemptions "should only be made where there is compelling evidence of the unworkability of competition or a clearly paramount social purpose." The Commission endorses that recommendation.

Some supporters of S. 1215 claim that the bill would merely be a clarification rather than an exemption. The Commission disagrees and suggests that the bill should be viewed as creating an exemption because it would exempt a single industry from one of the normal antitrust rules that apply throughout the economy.

Second, the Commission is unaware of any evidence establishing a need for this exemption from the antitrust laws. The Commission has seen no evidence suggesting that malt beverage wholesalers are different from wholesalers in other industries. They provide useful services—storage, refrigeration, and distribution services—Those services, however, are typical for wholesalers throughout the economy, especially in the food and beverage industries.

Proponents of S. 1215 have cited as one justification for the bill some uncertainty created by a California State court case that applied a per se standard to a vertical restriction in the liquor industry. The Supreme Court has recently decided that case, however, and it reversed the decision of the California court in such a way as to eliminate any fears or uncertainty that the companies in the malt beverage industry may have had.

Insofar as malt beverage wholesalers may be concerned about uncertainty involved in normal antitrust rule of reason analysis, the Commission would point out that flexibility is the strength of the rule of reason. The rule of reason allows triers of facts to take into consideration a great variety of evidence relating to the specific circumstances and peculiarities of an industry or company. Although there may be some uncertainty for brewers and malt beverage wholesalers, just as there may be some uncertainty for companies in any industry, the Commission believes that the advantages of using the flexible rule of reason outweigh such uncertainty. Furthermore, the novel standards of legality contained in S. 1215 could create a whole new area of uncertainty in the courts.

Third, because of the Supreme Court's holding in *GTE Sylvania*, S. 1215 would not change the legal status of procompetitive exclusive territorial arrangements. Such procompetitive arrangements are legal right now. The only arrangements that the bill could possibly legalize, therefore, are anticompetitive arrangements that are illegal under *GTE Sylvania*. The Commission's concern with this bill is that it could legalize restraints that could have serious anticompetitive effects and lead to higher consumer prices in some States.

Fourth, since the malt beverage industry is relatively highly concentrated at the brewing level and especially since State regulatory schemes typically create legal barriers restricting entry into the malt beverage industry, the enactment of S. 1215's exemption could unacceptably reduce the opportunity for market forces to correct any competitive problems which may exist or develop in the industry. Because of the relatively high concentration combined with the regulatory barriers to entry, significant consumer harm could result from allowing the malt beverage industry to use anticompetitive territorial restraints.

This last point highlights one of the differences between the malt beverage industry and the soft drink industry, for which Congress in 1980 enacted an exemption that appears similar to the one proposed in S. 1215. The Commission opposed that exemption as well and continues to believe it inappropriate, but it is nonetheless worth emphasizing that an exemption is particularly inappropriate for the malt beverage industry. Concentration in the soft drink industry was also relatively high, but in that industry there were no governmentally imposed barriers to entry that could prevent marketplace solutions to competitive problems. In addition, while the malt beverage wholesalers typically have investments in warehouses and trucks, their investments and risks are generally smaller than those of soft drink bottlers with their plants and equipment. Furthermore, malt beverage wholesalers are not engaged in the production of final malt beverage products, unlike the soft drink bottlers who do engage in production.

Finally, there is no FTC decision or any court decision which could be perceived as threatening the malt beverage industry.

Mr. Chairman, that completes the commission's formal statement. Before responding to any questions that you may have, I would simply like to call the committee's attention to the Commission's recent decision in the *Beltone* case, which involved vertical exclusive territorial restraints similar to those at issue in this bill. In that case, the Commission concluded that vertical exclusive territorial restraints are illegal only if they have some adverse interbrand effects.

The decision underscores why this bill is unnecessary: procompetitive territorial restrictions are currently legal. The decision also underscores why the bill, although it is called the "Interbrand Competition Act" would not promote interbrand competition, but would instead shield arrangements that can injure interbrand competition.

Thank you.

[The following was received for the record.].

Statement of
The Federal Trade Commission
Presented by

Walter T. Winslow
Deputy Director, Bureau of Competition

on

S. 1215
Malt Beverage Interbrand Competition Act

* * *

Committee on the Judiciary
United States Senate

August 5, 1982

Mr. Chairman, I would like to thank you for this opportunity to present the views of the Federal Trade Commission concerning S. 1215, the Malt Beverage Interbrand Competition Act. Attached to this statement is a copy of the Commission's June 11, 1982, letter to you, setting forth in detail the Commission's opposition to this bill. I respectfully request that the Commission's letter be included in the Committee's record. I would be pleased to answer any questions following the statement.

S. 1215 would legalize what are known as "airtight" vertical exclusive territorial agreements between brewers and wholesalers in the malt beverage industry provided there is "substantial and effective" interbrand competition.

Four points seem to the Commission to be especially relevant to the Committee's consideration of S. 1215.

1. Congress should require proof of the unworkability of competition as a prerequisite to enacting special antitrust exemptions.

2. The Commission is unaware of any such proof relating to the malt beverage industry, and—in fact—one of the principal reasons cited by supporters of S. 1215 has vanished as a result of the Supreme Court's recent decision in Rice v. Norman Williams Co.[1]

3. Procompetitive vertical territorial restraints are already legal under the Supreme Court's ruling in GTE Sylvania,[2] and therefore S. 1215 could only insulate conduct which is anticompetitive and currently illegal.

4. Because of existing governmental barriers to entry in the malt beverage industry, S. 1215 might reduce the opportunity for market forces to correct quickly any competitive problems in the malt beverage industry.

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[1] ____ U.S. ____ (July 1, 1982).

[2] Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36 (1977).

First, it is important to remember that the Supreme Court has called the antitrust laws the "Magna Carta of free enterprise,"[3] and as the Commission's letter indicates, "the antitrust laws reflect the Nation's fundamental policy in favor of free enterprise and competition." Significantly, the National Commission for the Review of Antitrust Laws and Procedures recommended that antitrust exemptions "should only be made where there is compelling evidence of the unworkability of competition or a clearly paramount social purpose."[4] The Federal Trade Commission endorses this recommendation.

Some supporters of S. 1215 claim that the bill would be merely a clarification rather than an exemption. The Commission disagrees, and it suggests that the bill be viewed as seeking to create an exemption because it would exempt a single industry from one of the normal antitrust rules which apply to virtually every other industry and company in the United States. As a proposed exemption, S. 1215 should be scrutinized under rigorous standards requiring clear evidence that potentially anticompetitive conduct should be permitted in order to achieve some fundamental social objective or to correct some otherwise-uncorrectable marketplace defect. Antitrust exemptions that do not meet such a standard erode business and consumer confidence in the integrity and fairness of the antitrust laws.

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[3] United States v. Topco Associates, 405 U.S. 596 (1972).

[4] National Commission for the Review of Antitrust Laws and Procedures, Report to the President and the Attorney General at 177 (1979).

Second, the Commission is unaware of any evidence establishing the need for this special exemption from the antitrust laws. The Commission has seen no evidence suggesting that malt beverage wholesalers are different from wholesalers in other industries. They provide storage, refrigeration, and distribution services that are typical for wholesalers, especially in the food and beverage industries. Nor has the Commission seen anything to indicate that competition is unworkable in the malt beverage industry or that there is any overriding social policy that could be served by this legislation. The proponents of S. 1215 have alleged as one justification for the legislation the fact that malt beverage wholesalers are caught between increasing concentration among brewers and increasing concentration among retailers. Even if this allegation were correct, however, it would not begin to establish that competition among wholesalers is unworkable or that exclusive territories would correct defects in the marketplace.[5]

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[5] Nationally, four-firm concentration in beer brewing has been increasing and is now about 68%. On a state-by-state basis the median four-firm sales figure exceeds 80%. Concentration among retailers, both nationally and in regional areas, is very low.

When exclusive territories exist, retailers have no opportunity to shop around for what they regard as the best deal for a particular product. A very important question is whether consumer welfare is better served by permitting any retailer to bargain with only one wholesaler rather than several for any particular brand of malt beverage. A single "yes" or "no" answer will not be correct in all circumstances. Instead, the answer may be different under different circumstances. The answer may change over time in a single geographic area as changes occur in the industry, in technology, and in distribution and marketing techniques.

Proponents of S. 1215 have also cited as a justification for the legislation the uncertainty created by a California case that applied a per se standard to a vertical restraint in the liquor industries. The Supreme Court has recently decided that case, Rice v. Norman Williams Co.,[6] and reversed the decision of the California court in such a way as to eliminate any fears that companies in the malt beverage industry might have had.

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[6] ____U.S.____ (July 1, 1982). Finding that a state "designation statute" authorized conduct that would be per se illegal under federal antitrust law, a California Court of Appeal had held the statute invalid on its face. The U.S. Supreme Court reversed and remanded on the ground that the statute authorized conduct which might be found legal under the correct antitrust analysis, i.e., under a rule of reason test. The decision should enable malt beverage wholesalers to rely on permissive state laws and a rule of reason analysis.

Insofar as malt beverage wholesalers may be concerned about any uncertainty involved with rule of reason analysis, the Commission would point out that flexibility is the strength of the rule of reason. The rule of reason, in other words, allows triers of fact to take into consideration a great variety of evidence relating to the specific circumstances and peculiarities of an industry or company. In addition, to prove an antitrust violation under a rule of reason test, the Government or the plaintiff must prove overall anticompetitive effects or injury. This requirement of proof must be contrasted to the irrebuttable presumption of adverse effects or injury in cases analyzed under a per se rule of illegality. The point to remember is that if a brewer or malt beverage wholesaler were to be charged with an illegal exclusive territorial arrangement, the Government or plaintiff in order to prevail would have to prove that the overall effect of the arrangement was unreasonably anticompetitive. Although there may be some uncertainty for brewers and malt beverage wholesalers--just as there may be some uncertainty for companies in any other industry--the Commission believes that the advantages of using the flexible rule of reason test outweigh such uncertainty. Further, the novel standards of legality contained in the bill could create a whole new area of uncertainty in the courts.

Third, because of the Supreme Court's holding in GTE Sylvania, S. 1215 would not change the legal status of procompetitive exclusive territorial arrangements in the malt beverage industry. Such procompetitive arrangements are legal. The only arrangements that the bill could possibly legalize, therefore, are anticompetitive arrangements that are illegal under GTE Sylvania. This point is simple, but it is also critical to an analysis of S. 1215. Under GTE Sylvania—which currently applies to the malt beverage industry—vertical non-price restraints that are overall procompetitive are legal while those that are overall anticompetitive are illegal. An exclusive territorial restraint in the malt beverage industry is legal if the restraint actually promotes competition through the procompetitive factors that the Supreme Court cited in GTE Sylvania.[7] At the same time, it is important to recognize that exclusive territorial arrangements can be harmful to competition and to consumers.[8] The Commission's concern with S. 1215, therefore, is that it would legalize some restraints that might have serious anticompetitive effects. In this regard, the bill might result in higher consumer prices in some states. It is important to remember that exemptions shield only conduct that would otherwise be illegal.

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[7] In GTE Sylvania, the Supreme Court listed several possible reasons why "[v]ertical restrictions promote interbrand competition by allowing the manufacturer to achieve certain efficiencies in the distribution of his products." 433 U.S. at 54.

> "For example, new manufacturers and manufacturers entering new markets can use the restrictions in order to induce competent and aggressive retailers to make the kind of investment of capital and labor that is often required in the distribution of products unknown to the consumer. Established manufacturers can use them to induce retailers to engage in promotional activities or to provide service and repair facilities necessary to the efficient marketing of their products. Service and repair are vital for many products, such as automobiles and major household appliances. The availability and quality of such services affect a manufacturer's goodwill and the competitiveness of his product. Because of market imperfections such as the so-called 'free rider' effect, these services might not be provided by retailers in a purely competitive situation, despite the fact that each retailer's benefit would be greater if all provided the services than if none did." Id. at 55 (citations omitted).

Fourth, since the malt beverage industry is relatively highly concentrated at the brewing level[9] and especially since state regulatory schemes typically create legal barriers restricting entry in the malt beverage industry, the enactment of S. 1215's exemption might unacceptably reduce the opportunity for market forces to correct quickly any competitive problems which may exist or develop in the industry. Because of the relatively high concentration combined with the regulatory barriers to entry, significant consumer harm could result from allowing the malt beverage industry to use anticompetitive territorial restraints.

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[8] By requiring a balancing of competitive harm and competitive benefit, GTE Sylvania recognizes the possibility that exclusive territorial arrangements can have overall net adverse effects on competition and consumers.

[9] See note 5, supra.

This point highlights one of the differences between the malt beverage industry and the soft drink industry, for which Congress in 1980 enacted an exemption[10] that appears similar to the one proposed in S. 1215. The Commission opposed that exemption as well and continues to believe it inappropriate, but it is nonetheless worth emphasizing that an exemption is particularly inappropriate for the malt beverage industry. Concentration in the soft drink industry was also relatively high, but there were no governmentally-imposed barriers to entry that could prevent marketplace solutions to competitive problems. In addition, while the malt beverage wholesalers typically have investments in warehouses and trucks, their investments and risks are generally smaller than those of soft drink bottlers with their plants and equipment. Furthermore, malt beverage wholesalers are not engaged in the production of final malt beverage products, unlike the soft drink bottlers who do engage in production. Nor is there any FTC decision or court decision which can be perceived as threatening the entire malt beverage industry.

Mr. Chairman, I would be pleased to answer the Committee's questions.

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[10] The Soft Drink Interbrand Competition Act, 15 U.S.C. §§ 3501-03.

FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

OFFICE OF THE CHAIRMAN

JUN 11 1982

Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

We appreciate the opportunity to respond to your recent request for the Federal Trade Commission's comments on S. 1215, the "Malt Beverage Interbrand Competition Act."

The Commission is strongly opposed to the enactment of S. 1215. We have just completed an analysis of H.R. 3269, the companion of S. 1215, and to expedite our response to your request we are enclosing copy of a letter to Chairman Rodino which explains the grounds for our opposition to this legislation in some detail.

In sum, we have concluded that this proposal is an unjustified special exemption from the antitrust laws, and that such proposals undercut the effectiveness of antitrust enforcement to preserve the free market economy. Moreover, since the agreements covered by the bill are currently permitted so long as they are procompetitive, the only possible effect of weakening the current antitrust standard would be to legalize arrangements that are predominately and demonstrably anticompetitive.

By direction of the Commission.

signed and hand-delivered

James C. Miller III
Chairman

Enclosures

FEDERAL TRADE COMMISSION
WASHINGTON, D. C. 20580

OFFICE OF THE CHAIRMAN

JUN 11 1982

Honorable Peter W. Rodino, Jr.
Chairman
Committee on the Judiciary
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

This letter responds to your request for the Federal Trade Commission's views on H.R. 3269 (the "Malt Beverage Interbrand Competition Act"), a bill that would create an antitrust exemption for certain exclusive territorial arrangements in the malt beverage industry. We have analyzed both the bill and the background material you sent us setting forth the position taken by supporters of the bill.

The Commission strongly opposes enactment of H.R. 3269 for two reasons. First, the bill is an unjustified special exemption from the antitrust laws for a single industry. As is discussed below, exemptions from the antitrust laws should not be granted unless there is clear evidence that enforcement of the antitrust laws in a particular situation would cause undesirable results. We are not aware of any such evidence concerning exclusive territorial arrangements in the malt beverage industry. Second, enactment of H.R. 3269 will not help either competition or consumers and may well injure both competition and consumers. Any procompetitive arrangements the exemption seeks to protect are currently permitted under well established principles of antitrust law. On the other hand, H.R. 3269's new and ambiguous standards are likely to create uncertainty, and -- more important -- the sole effect of weakening the current antitrust standards regarding exclusive territorial arrangements would be to legalize those arrangements that are predominately and demonstrably anticompetitive.

After a brief description of H.R. 3269, we explain the basis for our opposition to the bill. We believe that the reasons why enactment of the bill would not be in the public interest are apparent without the necessity of substantial analysis either of the nature of exclusive territorial arrangements or of competitive conditions in the malt beverage industry. Nonetheless, after explaining our reasons for opposing H.R. 3269, we set forth a more extensive analysis of these and other factors that may be useful to the Committee as background for considering this bill.

Description of H.R. 3269

The operative provision of H.R. 3269 is Section 2:

> "Sec. 2. Nothing contained in any antitrust law shall render unlawful the inclusion and enforcement in any written contract entered into after the effective date of this Act by any brewer, importer, trademark owner, or trademark licensee of a trademarked malt beverage with any wholesale distributor of provisions granting the wholesale distributor the sole and exclusive right to distribute and to sell such product in any defined geographic area within any State and limiting such exclusive distributor to the distribution and sale, directly or indirectly, of such product only for ultimate resale to consumers within that defined geographic area when such product is in substantial and effective competition with other malt beverage products within that defined geographic area."

The thrust of H.R. 3269 is to create an antitrust exemption allowing brewers and wholesalers to enter contracts defining the exclusive territory to be served by each wholesaler of a given brewer, provided that within each such territory there is "substantial and effective" competition with other malt beverage products. Section 3 of the bill recites that the bill is not intended to legalize the enforcement of exclusive territories "by means of price-fixing agreements, horizontal restraints of trade, or group boycotts, if such agreement, restraints or boycotts would otherwise be unlawful." Section 5 of the bill defines "malt beverage" to include beer, ale, porter, and other fermented beverages containing one half of one percent or more alcohol by volume.[1]

Special Antitrust Exemptions

In assessing proposed antitrust exemptions, it is important to recognize that the antitrust laws reflect the Nation's fundamental policy in favor of free enterprise and competition. Moreover, the antitrust laws are sufficiently flexible to take into account the different competitive conditions that prevail in different industries. For these reasons, exemptions from the antitrust laws are extremely difficult to justify. In this regard the Commission endorses the analysis and conclusions contained in the Report of the President's National Commission for the Review of Antitrust Laws and Procedures (1979), which declared (at p. 177) that antitrust exemptions are justifiable only where there is "compelling evidence of the unworkability of competition or a clearly paramount social purpose." The proffered justifications for an exemption presented by supporters of H.R. 3269 fall far short of this standard; therefore, the bill should not be enacted.

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[1] We have not analyzed market conditions to ascertain whether the assumption that there is a single malt beverage industry is in fact valid. For purposes of this letter, we assume that a single malt beverage industry exists.

The only evidence presented by supporters of H.R. 3269 concerning competitive conditions in the malt beverage industry consists of statistics tending to show that malt beverage wholesalers stand between two increasingly concentrated groups -- the brewers and the retailers.2/ Based on these statistics, it is claimed that the bill will maintain competition among wholesalers. Whether or not these statistics present an accurate picture of the malt beverage industry,3/ this claim does not appear to have any merit. We fail to see how exclusive territories in wholesaling could in any way offset any possible detrimental effects of an increase in concentration in brewing and/or retailing. (Moreover, as noted below, the antitrust laws already permit exclusive territorial arrangements to be used except in those situations where they have anticompetitive effects.) In short, we are not aware of even any colorable argument that the proposed exemption would remedy any defect in the marketplace and thereby promote either competition or other social goals.

In these circumstances, the antitrust laws should apply to the distributors of malt beverages in the same way that they apply to most of the rest of the Nation's economy. We believe that the antitrust laws deal with exclusive territories in a sound manner, but if the Congress desires to analyze this question, it should do so on a general rather than a special interest basis. Like the Soft Drink Interbrand Competition Act (15 U.S.C. §§3501-03) on which it is patterned, H.R. 3269 is an unjustified special exemption of the sort that erodes the role of antitrust enforcement as a guarantor of the efficient operation

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2/ This and other statements herein referring to the position of supporters of H.R. 3269 are based upon the undated memorandum, entitled "The Proposed Malt Beverage Interbrand Competition Act," which you sent the Commission together with your request for comments on H.R. 3269.

3/ As noted below, it does appear that concentration at the brewer level of the industry is high, but concentration at the wholesale level may be even higher.

of our free market economy, and the bill is inconsistent with recent actions and current proposals toward deregulation of the marketplace. In sum, H.R. 3269 should not be adopted because there is no principled basis for the antitrust exemption it would create.

Likely Effects of H.R. 3269

The second basis for our opposition to H.R. 3269 is that the bill will not help competition or consumers and may well injure competition and injure consumers. Exclusive territorial arrangements are frequently procompetitive but can sometimes be anticompetitive. Enactment of H.R. 3269 would apparently have the perverse effect of protecting exclusive territories that are anticompetive while not promoting exclusive territories that are procompetitive.

Under current law, exclusive territorial arrangements such as those covered by H.R. 3269 are lawful unless they have anticompetitive effects that outweigh their procompetitive effects. As stated by the United States Supreme Court in Continental TV, Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977), exclusive territorial arrangements restrict "intrabrand competition" but can promote "interbrand competition" and thus be procompetitive on balance. We elaborate on these points below, but for purposes of explaining our opposition to H.R. 3269 it is sufficient to reiterate that exclusive territorial arrangements are sometimes anticompetitive and to emphasize that such arrangements are judged on a rule-of-reason basis. As a result, exclusive territorial arrangements are currently legal except in those circumstances in which it is proved that their overall effect is anticompetitive.

Under H.R. 3269, however, the antitrust laws would be inapplicable to an exclusive territorial arrangement in the malt beverage industry whenever the products covered by the arrangement are in "substantial and effective competition" with other malt beverage products. It is not clear what this statutory language is intended to mean,[4] but it is evident to us that any weakening of the antitrust standard of legality would be undesirable. Since antitrust law currently outlaws only those arrangements that are anticompetitive, the only exclusive territorial arrangements that could be legalized by H.R. 3269 are those that are predominately and demonstrably anticompetitive.5/

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[4] For example, portions of the legislative history of the Soft Drink Interbrand Competition Act suggest that it did not create a legal standard different from the antitrust laws. See, e.g., H.R. Rep. No. 1118, 96th Cong., 2d Sess. 4-5, 16 (1980); 126 Cong. Rec. H5534 (daily ed. June 24, 1980). However, some legislative history supports a contrary result (see 126 Cong. Rec. at H5536-37), and one court has held that the act created a different standard of legality. Coca-Cola Co. v. FTC, 642 F.2d 1387 (C. Cir. 1981).

Moreover, we do not believe that enactment of H.R. 3269 would promote those exclusive territorial arrangements that are procompetitive. In this regard, we disagree with assertions made by supporters of H.R. 3269 that the bill will have the beneficial effect of reducing uncertainty about legal requirements or reducing the costs of litigation.6/ At present, the legality of exclusive territorial arrangements is tested by well established legal and economic principles, and H.R. 3269 would introduce new and ambiguous criteria that would have to be applied by both firms in the industry and by courts and the Commission. The result of such a change is likely to be increased uncertainty and increased costs of litigation, and the bill will therefore not promote -- and may even discourage -- the establishment of procompetitive exclusive territorial arrangements.

In sum, H.R. 3269 should not be enacted because it will not help either competition or consumers, and it may well injure both competition and consumers.

5/ Section 3 of the bill provides that it does not legalize "enforcement" of exclusive territorial restrictions by means of "price-fixing arrangements, horizontal restraints of trade, or group boycotts." Section 3 in no way lessens our opposition to H.R. 3269, because this provision in no way alters the fact that the only effect of weakening the current antitrust standard would be to legalize arrangements that are anticompetitive.

6/ The sole basis for the claim that there is a need for legislation to provide greater certainty in this area is the opinion in one California case, and that case is currently being reviewed by the United States Supreme Court. Norman Williams Co. v. Rice, 1980-2 Trade Cas. ¶63,484 (Cal. Ct. App.), cert. granted, 50 U.S.L.W. 3447 (U.S. Nov. 30, 1981) (No. 80-1012). We do not believe this case creates uncertainty about the proper antitrust analysis of exclusive territorial arrangements. We also note that we see no merit in the totally unsupported claim made by supporters of H.R. 3269 that the bill would provide beneficial confirmation of the regulatory authority of the states. So far as we are aware, there is no reason to question the states' full regulatory authority in this area. If any such question existed, H.R. 3269 would not remedy it since none of the bill's provisions deal in any way with state regulation of the malt beverage industry.

Supplemental Analysis of Exclusive Terriorial Arrangements in the Malt Beverage Industry

As noted above, analysis of the likely effects of H.R. 3269 does not require any substantial discussion either of exclusive territorial arrangements or of competitive conditions in the malt beverage industry. Nonetheless, we are including such a discussion as background for the Committee. The discussion serves to emphasize the lack of justification for H.R. 3269.

We begin by emphasizing that exclusive territorial arrangements can be procompetitive in that they can be used by a manufacturer to avoid problems that sometimes arise if its distributors directly compete among themselves. For example, a manufacturer may want its distributors to take steps to preserve product quality or to provide promotional or other services. For some products, distributors' expenditures on such activity can enhance demand, promote interbrand competition, and in general contribute to the product's overall success. If the manufacturer's distributors compete among themselves, however, each distributor may seek to avoid making these procompetitive expenditures and to profit from whatever increased sales are generated by the expeditures of its competitors. In other words, each distributor may seek to take a "free ride" on its competitors' expenditures, in which case procompetitive services may ultimately not be provided.

When a manufacturer is concerned that its distributors may not voluntarily provide services because of a "free rider" problem, the manufacturer may respond in a variety of ways to ensure or encourage the provision of the services it desires. The manufacturer can ensure that the services will be provided by performing them itself or by contracting with distributors to perform the services. Alternatively, the manufacturer may seek to provide distributors with an increased incentive to perform the services by such means as assigning them areas of primary responsibility or exclusive territorial arrangements. By adopting these policies, the manufacturer restricts or eliminates intrabrand competition, and interbrand competition may thereby be increased because distributors protected by these policies may have a greater incentive to provide services since their expenditures will benefit them and not their competitors.

Although exclusive territories necessarily restrict intrabrand competition, they do not necessarily or even usually provide market power to distributors. As noted above, there are a variety of less restrictive means by which a manufacturer may be able to ensure that necessary services are provided, and the manufacturer would normally have an incentive to avoid granting exclusive territories in circumstances where the distributor would thereby be able to exercise market power. The existence of these alternatives and incentives provides some protection against the danger that the assignment of an exclusive territory will result in higher prices caused by a unilateral exercise of market power by a distributor. Moreover, there is little risk that any of a manufacturers' distributors will be able to restrict distribution and raise prices if they all face vigorous competition from the distributors of competing producers.

There are, however, additional ways in which exclusive territorial arrangements can be anticompetitive. In particular, such arrangements can facilitate or reinforce collusion among competitors. For example, distributors may wish to enter into a horizontal market division agreement in which there will be only one distributor in each area. The purpose of this agreement is not efficiency in distribution, but the elimination of competition so that distributors can charge prices above the competitive level. Such an anticompetitive agreement among the distributors could be facilitated by exclusive territorial arrangements between manufacturers and distributors. In this example, the anticompetitive effects would in no way be diminished by the existence within each territory of competition among the products of different manufacturers.

As noted above, manufacturers normally do not have an incentive to use exclusive territorial arrangements when they are likely to permit distributors to restrict output and raise prices, but manufacturers will not always be adverse to exclusive territories established for reasons other than efficiency. The manufacturers themselves may wish to collude in order to restrict output and raise prices, and their collusion will not be fully effective unless they are able to prevent entry. The colluding manufacturers may therefore be willing to share their higher profits with the existing distributors to obtain their agreement that they will not distribute the products of any non-colluding manufacturers. In this situation, the exclusive territorial restrictions reinforce a clearly anticompetitive agreement.

The competitive conditions of many industries are such that it is relatively difficult for firms to use exclusive territorial arrangements in anticompetitive ways. When concentration levels and entry barriers are low, for example, collusion among competitors is difficult to enforce and is likely to generate new entry. On the other hand, high concentration and high entry barriers make it more likely that exclusive territorial arrangements will be used in an anticompetitive manner.

Before turning to a brief discussion of the malt beverage industry, we wish to emphasize that one cannot justify an antitrust exemption for a particular industry on the basis of evidence that competitive conditions in all or part of the industry make it relatively difficult for firms to use exclusive territorial arrangements in an anticompetitive manner. There are many industries in which such anticompetitive conduct may be difficult, and the antitrust laws serve a useful function in these industries by outlawing anticompetitive arrangements while permitting procompetitive arrangements.

Moreover, it appears that competitive conditions in the malt beverage industry are such that there are particular reasons for concern that exclusive territorial arrangements could be used in anticompetitive ways. The Commission's Bureau of Economics published a report on the brewing industry in 1978.7/ According to that report and more current publicly available information, the brewing industry is quite highly concentrated. Four firm concentration increased at the national level from 46 percent in 1970 to 63 percent in 1977, and we understand that it now exceeds 68 percent. Moreover, in most states, four firm concentration exceeds 80 percent. We also understand that wholesale concentration is high -- perhaps higher than brewer concentration -- though we do not have reliable data on the structure of the malt beverage wholesale distribution sector. Finally, we understand that the laws of many states create entry barriers that restrict entry into the wholesale distribution of malt beverages. These facts do not indicate that there are necessarily any significant competitive problems in the malt beverage industry,8/ but the combination of high concentration and state-created entry barriers do make this an industry in which it is particularly important to safeguard against anticompetitive conduct such as collusion among brewers or wholesalers. In these circumstances, the proposed exemption seems particularly undesirable because it would increase the likelihood that exclusive territorial restrictions will be used to suppress rather than enhance interbrand competition.

7/ FTC, The Brewing Industry: Staff Report of the Bureau of Economics (1978).

8/ Indeed, the Bureau of Economics' 1978 report concluded that the brewing industry was generally competitive.

The Commission is unable to compare the distribution of malt beverages to soft drink bottling in any ways that are useful to a consideration of the likely effects of H.R. 3269. Obviously, the costs incurred and risks faced in these industries differ substantially, and the activities typically undertaken by soft drink bottlers undoubtedly differ from those engaged in by malt beverage distributors. For example, soft drink bottlers participate in both the production and distribution of soft drinks, and they must bear the cost of transporting finished soft drinks over substantial differences. Malt beverage distributors, on he other hand, perform only a wholesaling function and ap ently face lower costs than soft drink bottlers. These di rences, however, are not particularly relevant in d mining the likely effects of H R [illegible]69.

Conclusion

The Commission is strongly opposed to the adoption of H.R. 3269. We are unaware of any evidence or principled argument that might justify the bill, and we believe that enactment of such unjustified special exemptions has the detrimental effect of undercutting the ability of antitrust enforcement to preserve this Nation's free market economy. Moreover, since the antitrust laws currently permit procompetitive exclusive territorial arrangements, the only exclusive territorial arrangements that could be legalized by a weakening of current antitrust standards are those arrangements whose overall effect is anticompetitive. Finally, our view of competitive conditions in the malt beverage industry serves to reinforce our opposition to H.R. 3269, for the industry appears to be one in which it is particularly important to safeguard against the anticompetitive use of exclusive territorial arrangements.

By direction of the Commission.

Signed and hand-delivered

James C. Miller, III
Chairman

The CHAIRMAN. Thank you.

I have a few questions, if you will respond to those. What has been the FTC's experience with the operation of exclusive territories in the soft drink industry since passage of the soft drink industry last Congress?

Mr. WINSLOW. Mr. Chairman, the soft drink bill preserves the status quo. It prevented from going into effect a decision by the Commission which would have changed the structure of the soft drink bill. Therefore, we cannot say that prices rose because of the Soft Drink Interbrand Competition Act. We can say that the soft drink bill prevented us from finding out whether prices would have gone down if a rule of reason had continued to be applicable in the soft drink field.

The Commission has done no formal study in this area. We have received some consumer complaints. We received recently a congressional letter, enclosing a constituent's complaint. In that case, the constituent was a small businessman who owned two convenience stores that were located not too far from each other. He sent cases of a particular soft drink from one of his stores to his other store, and his two retail stores happened to be in different wholesalers' territories. One of his wholesalers was charging him $2.50 more per case than the other wholesaler, so what he was trying to do was buy from the cheaper wholesaler and send the soft drink over to his other store. He was terminated by the low-price bottler for that practice. However, the Commission conducted no real investigation in that instance, primarily because of the soft drink bill and the exemption that the bill created.

The CHAIRMAN. Now, the soft drink bill has become law.

Mr. WINSLOW. It has.

The CHAIRMAN. How would you draw the distinction between that bill and this, or how would you justify having one on the books and not the other?

Mr. WINSLOW. I think that there are some differences in the language of the two bills, but the most important thing to me, Mr. Chairman, is that the existence of governmental entry barriers in the malt beverage field makes exclusive territories much more potentially dangerous in that industry than they are in the soft drink industry. There are some other differences, too. Soft drink bottlers engage in production, whereas malt beverage wholesalers perform a more routine, though important, wholesaling service. But the most important factor, I would urge, is the existence of state laws, which already prevent some competition in the liquor and malt beverage fields.

The CHAIRMAN. Do you believe that the passage of state legislation permitting exclusive territories in the beer industry provides any protection to brewers and wholesalers who establish such territories against actions under the Federal antitrust laws?

Mr. WINSLOW. Whether or not there are State laws that permit exclusive territories, most exclusive territorial arrangements are legal under the Federal antitrust laws in any event. We are talking here about a kind of arrangement that is to be judged under the rule of reason, and when the exclusive territories are serving a useful purpose for, in this case, the brewer—usually, one would say the manufacturer, but here we are talking about brewers—if the territorial arrangement is truly serving the brewer's interest in providing a quality product to consumers, the arrangements are likely to be legal, regardless of State law.

The CHAIRMAN. What impact do you think the decision in the *Rice* v. *Norman Williams* case has had on the legality of exclusive territories in the beer industry?

Mr. WINSLOW. I think, sir, it has clarified that rule of reason analysis will be used to judge these kinds of restrictions, which means that when they do serve legitimate functions, they are legal. The *Rice* case, as it was decided by the California court, used a per se analysis. That approach was, frankly, thought to be incorrect by most antitrust authorities. The United States filed a brief in the Supreme Court, pointing out that the rule of reason analysis was appropriate here. And the importance of the *Rice* case to this situation is that it gives brewers and malt beverage wholesalers assurance that procompetitive territorial restrictions can exist.

The CHAIRMAN. One reason given to justify the need for exclusive territories in the beer industry is the practice of transshipping. Does the Commission view transshipping as a matter of concern?

Mr. WINSLOW. It would be of concern to the extent that transshipping causes problems—for example, stale beer might be shipped from one territory to another, and I know that is frequently given as an example of why exclusive territories are important. My point would be, Mr. Chairman, that to the extent that transshipping really does create those kinds of problems, prohibitions on transshipment will be considered in the rule of reason analysis, and the prohibition can be found to be lawful, even under the rule of reason, and therefore, this bill is not necessary.

The CHAIRMAN. I think that covers my questions. We thank you very much for your presence and the contribution you have made to the hearing.

Mr. WINSLOW. Thank you, Mr. Chairman.

The CHAIRMAN. Our next witnesses constitute a panel. Eleanor Fox, professor of law, New York University Law School, and Willard F. Mueller, professor of agricultural economics, University of Wisconsin, if you will come around and have a seat.

Is Professor Mueller here?

[No response.]

The CHAIRMAN. I do not believe he is here, so we can proceed with you, Ms. Fox.

STATEMENT OF ELEANOR FOX, PROFESSOR OF LAW, NEW YORK UNIVERSITY LAW SCHOOL, NEW YORK, N.Y.

Ms. FOX. Mr. Chairman, I am very pleased to be here today, and thank you very much for giving me this opportunity. I would like to address two points briefly, the States rights point, and, in a little more detail, the competition point. I strongly oppose the bill, because I think it would authorize millions of dollars of consumer harm and the Justice Department and the FTC will be powerless to do anything about it.

First, as to States rights, I note that Senator Proxmire, in introducing the bill, and later in testifying for the bill, explained that the main purpose of the bill is to clarify the 21st amendment. I agree with Mr. Winslow that *Rice* v. *Norman Williams Co.* eliminates any need to clarify the right of States to regulate the transportation and flow of alcoholic beverages within the State. The case confirms what is now clear law. The States have virtually every right to regulate alcohol within their borders, except that they cannot tell private parties that the private parties can go out and violate the antitrust laws and the State will immunize them. That is all the States cannot do.

It seems to me that there is no real State rights issue unless one is basically hostile to a Federal antitrust law and wishes to give antitrust back to the States.

As for the competition issue, which is the crux of the bill, I think, Senator, that the real question is whether airtight exclusive territories for the distribution of beer will virtually always increase interbrand competition and virtually never decrease it and harm the consumer. It would seem to me inappropriate for Congress to give a blanket authorization for airtight territories unless that is the case.

In order to examine whether that is the case, we can look at actual experience, and we can make predictions by usual forms of antitrust analysis. As for actual experience, we have the experience of Indiana. Indiana had authorized exclusive airtight territories, and then eliminated them. Prices dropped 20 percent and competition and service increased dramatically.

Let me turn, now, to antitrust analysis. *GTE Sylvania* is our principal guide, and the recent FTC *Beltone* case is an additional guide. By antitrust analysis, we can make a predictive judgment as to whether competition will be lessened and consumers hurt.

The basic problem in antitrust is to prevent artificial price rise over cost and to prevent inefficiently high cost, and we count on competition to do both things.

There are two ways in which we can get an artificial rise in price above cost, even where there is interbrand competition. One way is, if the firms were allowed under law to do it, the distributors could form a cartel. They could have an agreement actually fixing price among them. This, as we know, is illegal per se. The bill does not authorize it. It is illegal per se and a criminal violation because of its pernicious effect on competition and the consumer.

There is one other way in which that same pernicious effect can be achieved, and that is by what we call interdependence. It requires very special market conditions. There must be very few firms in the market. There must be inelastic demand, meaning buyers cannot readily shift their demand even if price should rise. There must be high barriers, meaning other suppliers cannot easily enter that market even if price should rise. And there must also be no destabilizing effect, like a pricecutter, such as a transshipper, that would cause competition to break out. Under these very narrow circumstances, by interdependence, without any agreement, the producers or distributors in the field could coordinate their price, maximize their profits, and cause exactly the same pernicious effect, that underlies the criminal per se rule.

Of course, interdependent behavior is not an illegal, horizontal restraint, because there is no agreement. The antitrust law can address such behavior by enforcing the law against vertical agreements that facilitate it. It seems to me that the question before Congress is whether beer distribution exhibits the market characteristics that breed interdependence, because if it does, there is a real danger that exclusive airtight territories, will facilitate harm to consumers.

I believe that the answer is yes; that the beer industry does exhibit these characteristics, and that airtight territories could pose a serious risk. There are high concentration and high barriers. Concentration is even higher in some regional areas than nationally. Is higher in wholesaling than brewing, because some brewers appoint a single distributor; that is, two or more brewers might appoint one distributor, leading to fewer firms at the distributor level and a greater opportunity to coordinate.

Now, I am not arguing that Congress should determine that airtight restraints in beer distribution are illegal, but simply that there is a serious danger that these restraints will hurt the consumer and that a clean bill of health by Congress in advance of case-by-case examination is not in the public interest.

It is argued that free-rider effects should be balanced against any anticompetitive effects. There is not, in my view, a serious free-rider problem. The brewers do almost all of the advertising, so there is no problem of distributors taking a free ride on other distributors' advertising.

Basically, the bill heralds a return to a kind of fair trade. We had fair trade under Miller-Tydings, and that law was repealed. Incidentally, in enacting Miller-Tydings, Congress apparently thought that interbrand competition would protect the consumer, because that statute allowed retail price-fixing only if the price-fixed article was in "free and open" competition with other brands. Yet, when Miller-Tydings was repealed, prices fell 20 percent. I think there is a similar danger here that this bill will dampen competition. The question is, Who should get 20 cents of every dollar of the price of beer—brewers and wholesalers, or consumers?

Thank you, Mr. Chairman.

The CHAIRMAN. I would like to ask you a similar question that I propounded to the last witness. We now have a law somewhat similar to this for soft drinks. How do you distinguish between the effects of that law as compared with the effects of this law if it were enacted?

Ms. FOX. Mr. Chairman, I believe that the beer bill can have similar effects, and it worries me. The question I would ask is, What next? We are depriving our Government enforcement agencies from the chance to look to see if anticompetitive effects arise from vertical restraints under future sets of facts. We are doing it in beer; we have done it in bottling. Everybody will want a similar exemption. This bill works on the premise that airtight exclusive territories when there are more brands than one simply ought to be legal per se. And I think that would be very dangerous. I think we should stop here before we expose the consumer to yet greater harm.

The CHAIRMAN. Some people feel the soft drink bill is different from this bill, that it had some merit, and that it has not had detrimental effects.

Ms. FOX. Yes, Mr. Chairman. I am really not prepared to address the differences. It is true that the beer industry is more highly concentrated and State regulation creates higher barriers to entry, so that the beer bill could be expected to do more consumer harm than the bottlers' bill. But both are special exemptions where, in my view, no case for exemption has been made.

The CHAIRMAN. If you care to submit anything on that, we would be glad to have it for the record.

Ms. FOX. Yes. Thank you.

The CHAIRMAN. You see, those who favor this bill feel that, since we have done this for the soft drinks, why not do it for this industry. On the other hand, there are others who say there is a vast difference, that soft drinks are in a different category, and therefore it should not be done.

So anything else you could add or send to us on that point, we would be glad to receive.

Ms. FOX. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you very much for your testimony.

Ms. FOX. Thank you.

[Prepared statement follows:]

Statement of

Eleanor M. Fox

on S. 1215,

the Malt Beverage Interbrand Competition Act

Mr. Chairman and Members of the Committee:

My name is Eleanor Fox. I am a professor of law at New York University School of Law. I have served as a member of the National Commission to Review Antitrust Laws and Procedures, and as Chair of the Antitrust Law Section of the New York State Bar.

I am most pleased to accept the invitation to appear before the Committee to testify on S. 1215, the Malt Beverage Interbrand Competition Act.

I strongly oppose the bill. Either it would codify existing law, in which case it would be superfluous, or it would grant an exemption from the Antitrust Laws, in which case it would harm consumers.

The principal provision of S. 1215 is Section 2. Section 2 provides that nothing in the Antitrust Laws shall render unlawful an agreement between any brewer of a trademarked malt beverage and any wholesale distributor granting the distributor the exclusive right to distribute in any defined geographic area in any state, and limiting such distributor to distribution only for ultimate resale to consumers within that geographic area, "when such product is in substantial and effective competition with other malt beverage products within that defined geographic area."

Section 3 provides that Section 2 does not legalize enforcement of provisions described in Section 2 by means of otherwise unlawful "price-fixing agreements, horizontal restraints of trade, or group boycotts."

Senator Proxmire, who with Senator Kasten first introduced the Bill last year, states that the main purpose of the Bill is to clarify the Twenty-First Amendment to the Constitution of the United States, to assure that states can act to control the territorial system of distribution within their states. Senator Kasten, in his recent testimony before this Committee, stressed also that the Bill is designed to promote "_fair_ and vigorous interbrand competition," and will provide "_security_ to wholesalers and at the same time promote vigorous interbrand competition" (emphasis mine).

The proponents in general, and particularly the exclusive wholesale distributors in favor of airtight territories,[1] argue that low-priced intrabrand competition across territorial lines erodes quality, lessens distributors' incentives to promote and advertise, threatens their profit margins, makes it uneconomic to service small accounts, and will cause the demise of traditional distributors and resulting loss of employment. They argue that the state of the Antitrust Law leaves them subject to costly litigation, whereas it is clear, they conclude in effect, that territorial restraints in beer distribution are legal _per se_.

Since most of the testimony in support of this bill was offered, a major Supreme Court decision has eliminated any need to clarify the Twenty-First Amendment. In _Rice v. Norman Williams Company_, 1982-2 Trade Cas. ¶64,816 (Sup. Ct. 1982), the Supreme Court held that the Antitrust Laws are no bar to a state statute that prohibits liquor importers from accepting delivery of any brand unless they are authorized to do so by the distiller. It is clear law that the state has every right to control the transportation and distribution of alcoholic beverages within its borders, even if the state-directed and supervised regulation is anti-competitive. All that the state cannot do is authorize private parties to make agreements that unreasonably restrain trade and immunize those parties from suit under the Antitrust Laws. California Liquor Dealers v. Midcal Aluminum, Inc., 445 U.S. 97 (1980); Schwegmann Bros. v. Calvert Corp., 341 U.S. 384 (1951).[2]

The remaining question is the competition question. I would frame it as follows: Have the proponents of the legislation made a convincing case that, given unique qualities of the beer industry, airtight territories for wholesale distributors will always, in all geographic areas, increase interbrand competition, or at least virtually never harm interbrand competition and raise the price to consumers?

This is the appropriate question because, if substantial harm to consumers is threatened in some markets and under some conditions, it would be bad public policy for this distinguished body to facilitate that harm by a blanket exemption. Conversely, it would be good public policy to continue to enable our enforcers to scrutinize territorial restraints in the framework of existing market realities, and to decide if and when, under the GTE Sylvania rule-of-reason standard, restraints threaten consumer harm.[3]

The proponents of the Bill have not made their case. To put it another way, S. 1215 will almost surely allow harm to occur to consumers, and our Justice Department and FTC will be powerless to stop it. This is clear from both fact and theory. The fact is that Indiana had and repealed exclusive sales territories; prices dropped more than 20%, and service improved dramatically.[4]

As for theory, or the analytical framework within which to predict competitive effect, let me refer to the analysis suggested by GTE-Sylvania, set forth in the letter of Assistant Attorney General McConnell to Chairman Thurmond of April 13, 1982, and endorsed by the Office of the Assistant Attorney General in Charge of Antitrust. The purpose of the analysis is to identify those situations in which the consumer will probably be hurt because price will rise and output will be restrained.[5]

The question is, under what market circumstances are exclusive territories likely to cause an artificial price rise, rewarding producers with excessive profits or protected inefficiencies, and exploiting consumers? There are at least two ways in which this artificial price rise can happen, when the product is in competition with other brands. One way is by an agreement among the wholesalers. They could, if the law let them, agree to a higher price. This is called a price-fixing agreement or a cartel. It is illegal per se because of its pernicious effect on consumers; it is a criminal violation, and the Bill does not weaken this law. However, there is another way in which this same evil effect can result.[6] It can result only under special market conditions. There must be very few sellers in the market; consumers must have a strong preference for the good and be disinclined to shift their purchases substantially if price should rise, and barriers to entry must be high, so that potential suppliers could not easily shift their resources into the market to take advantage of the profit opportunities if price should rise. Also, there must be no destabilizing forces, like transshippers, who trigger price competition. Under these market conditions, producers or wholesalers know that they will all be better of if they keep prices high, and they will all be worse off if they price-compete. Since they are few in number, price coordination is relatively easy. They can observe one another's prices and maximize their joint profits, without any agreement among them. This is called interdependent behavior, and it is not illegal as a horizontal restraint because there is no contract, combination, or conspiracy to price-coordinate. Yet this behavior produces exactly the same pernicious effect on consumers as the criminal price-fixing violation. Vertical restraints that facilitate this effect are probably illegal under a rule of reason.

Accordingly, we should ask, as to beer: Are the market conditions necessary to the price-elevating effect present or likely to be present in some beer markets? The answer seems to be yes. In 1980, the top two brewers had 50% of the national market. Four-firm concentration exceeded 80% in 30 of 39 states for which data was available. Concentration in wholesaling is even higher than concentration in brewing because more than one brewer appoints the same distributor, making price-coordination at the distributor level easier than at the producer level. Barriers into distribution are unusually high. The Department of Justice concludes in its letter to the Chairman: "[T]his industry appears to be one in which the risk that widespread use of exclusive territories may produce anticompetitive effects is almost uniquely high." Letter, supra, at 4.

Given increasing concentration by merger in the brewing industry, this risk is likely to increase.

Let me return, now, to arguments of proponents of the Bill, which become relevant at this stage of the analysis. I think we have to assume that, with airtight territories, artificial price-rise through interdependent behavior in some beer markets in the near future years is a danger that cannot be discounted. Proponents of S. 1215 assert that exclusive territories are needed, nonetheless, to preserve quality, prevent free rides on promotion, and prevent cream-skimming by transshippers, and thereby make interbrand competition more effective. Are these claims good defenses, and should they be; and are they factually so persuavise at this stage of development of the information and evidence before Congress that Congress should declare as a blanket matter that the case is made?

Let us look at the claims. Proponents of the Bill claim that less-than-closed territories will produce an intolerable free ride and will inefficiently lessen the promotional efforts of the distributors. But in fact promotion is done by the brewers.[7] The brewers spend tens or hundreds of millions of dollars a year on advertising.[8]

Proponents claim that, under a regime of open territories, the brewers will be unable to control the freshness of their beer. But the brewers do control freshness by requiring that free market wholesalers (in Indiana, which abolished territories) complete and file forms specifying date of delivery and other information.[9] Moreover, the brewers can quite easily date each can with a date (rather than a code) that retailers can read.[10]

Finally, proponents claim that transshippers are skimming the cream of their sales by making large drop-shipments at low prices. This is a claim of different color. This is a claim that free territory wholesalers, who are able to realize the efficiencies of innovative systems of distribution, are out-competing the territory-bound distributors.[11] It is a claim that competition itself is unreasonable. This, said Justice Stevens for the Court in United States v. National Society of Professional Engineers, 435 U.S. 679, 696 (1978), will not be heard to justify an anticompetitive restraint. This, I think, is the right and necessary principle to protect consumers.

In sum, there is a risk that brewers' territorial restraints, in some markets, under some circumstances, will contribute to an artificial price rise that will not be outweighed by free rider, freshness, or transshipper justifications. Perhaps it is exactly this risk that inspires the industry to seek protective legislation. But if that is so, then Congress must ask itself this question: Who should get 20¢ out of every dollar of the price of beer -- the less efficient wholesaler, or the consumer?

FOOTNOTES

1 An airtight territory is a territorial allocation to one distributor alone. No other distributor of the brand is allowed in, and the designated distributor is not allowed out.

2 If S. 1215 were, as Senator Proxmire states, truly states' rights legislation, one would have expected the Bill at least to overrule Midcal and thus allow states to direct resale price-fixing of alcoholic beverages. One suspects that S. 1215 does not go so far because the public knows, from the recent experience of repeal of the fair trade laws and the 20% price drop as states moved to a competitive environment, how costly "fair trade" is to the consumer. See, for data regarding the price drop, Waldron, "Foes Map Liquor War Tactics, N.Y.T., Sun. Jan. 14, 1979, § XI, p. 1, col. 1; Sullivan, "Jersey Will Remove Liquor Price Rules," N.Y.T. Jan. 3, 1979, p. 1, col. 1.

Moreover, in view of the fact that the sponsors present the bill as one about healthy competition rather than about evils of alcohol, if the real purpose of this bill were states' rights, one would have expected the bill were to all industries; not just beer.

3 See In Re Beltone Electronics Corp., July 6, 1982 FTC, BNA Antitrust & Trade Reg. Rep., July 8, 1982, p. 112 et seq., esp. 124-26, wherein the FTC scrutinized and held legal territorial restraints in the hearing aid industry. The market was competitive and interbrand competition was not harmed.

4 Report of legislative study commission in Indiana, cited in Statement of Alabama Retail Association on S. 1215. See also Testimony of the Indiana Retail Grocers Ass'n, June 21, 1982.

5 The claim that the consumer will be protected by the requirement in the Bill that the product must be "in substantial and effective competition with other malt beverage products" in the geographic area cannot be taken

seriously. The Miller-Tydings Act, which authorized the state fair trade laws (resale price-fixing) had nearly the same language. It required that the commodity be "in free and open competition with commodities of the same general class produced or distributed by others." It was assumed that where other brands were available, the interbrand competition would protect the consumer. It is of course well known that the interbrand competition did not protect the consumer. When fair trade was repealed and state resale price-fixing statutes were voided, prices fell about 20%. See note 2 supra.

6 Even without collusion, the retailer and the consumer may be harmed by the inherent inefficiencies built into the system of airtight territories. As Matthew Protos, President of the National Licensed Beverage Association, explained in his June testimony, a retailer may be located near Wholesaler A, who has reasonable prices and offers quick delivery but is assigned to another territory. The retailer has no choice as to where to buy the brand, and must take it, if at all, from the much more distant assigned Wholesaler B, at a higher price. The retailer then has to compete with the nearby retail customers of Wholesaler A.

7 See Testimony of Richard M. Quinn, Vice President, Indiana Malt Beverage Association, June 21, 1982:

> "I was told by a Miller Brewing Company official that advertising was the brewery's responsibility and was informed that the brewery would create the consumer demand and our job was to establish and maintain maximum distribution to fill the demand."

See Exclusive Territorial Distributorships and Consumer Welfare: The Case of Beer, prepared by the National Institute of Economics and Law, June 21, 1982, p. 26-28.

8 National Institute report, supra, 26.

9 Testimony of Richard M. Quinn, supra.

10 See National Institute report, supra, 29.

11 Mr. Joseph A. Lackey, President of the Indiana Retail Grocers Association, points out that transshippers are the best spur to competitive performance. Testimony, June 21, 1982.

The CHAIRMAN. As our next witnesses, we have a panel, I believe, of Raymond J. Justak, vice president of Todd & Justak, Indianapolis, Ind.; Matthew R. Dee, president of United Beverage Co., South Bend, Ind.; and James W. Riddell, Dawson, Riddell, Fox, Holroyd & Wilson, Washington, D.C.

I believe you gentlemen favor this bill?

Mr. JUSTAK. Yes, we are in favor of this bill.

The CHAIRMAN. We will be pleased to hear from you at this time.

STATEMENT OF A PANEL, INCLUDING RAYMOND J. JUSTAK, VICE PRESIDENT, TODD & JUSTAK, INDIANAPOLIS, IND.; MATTHEW R. DEE, PRESIDENT, UNITED BEVERAGE CO., SOUTH BEND, IND.; AND JAMES W. RIDDELL, DAWSON, RIDDELL, FOX, HOLROYD & WILSON, WASHINGTON, D.C.

Mr. JUSTAK. My name is Raymond J. Justak. I am the vice president of Todd & Justak, and I am the former president of the Beer Distributors of Indiana, which is a trade association that represents beer wholesalers, and we have approximately 134 members.

I am appearing on behalf of the Beer Distributors of Indiana, Inc., in favor of Senate bill 1215. I have a prepared statement that was submitted for the record, and in the interest of time, I will just highlight that statement. I also have an article from the newspaper——

The CHAIRMAN. Without objection, your entire statement will go into the record following your oral remarks. Now, what did you want done with that article?

Mr. JUSTAK. Put that in the record, too. It is just an article from a typical retailer, giving his opinion of——

The CHAIRMAN. Without objection, we will put that in the record. You may proceed.

Mr. **Justak**. In Indiana, we have probably had transshipping existing longer than anyplace else, and it has been going on about 5 years, and our State is in a horrendous condition. Fully 75 percent of our wholesalers are about to go under. What we have got is a situation where we have got very destructive, unfair competition. We are bound by contractual agreement with the brewers to service our own primary area of responsibility. Under that agreement, we are required to service every retailer in our community, whether he buys one case a week or 100 cases a week. And we not only have to deliver to him at least once a week and have our salesman call on him, per the brewery agreement, but we also have to hang point of sale, and we have got to take care of draft beer, which normally, you have got a lot of service connected with it, and it is not profitable.

So we start with the premise that we have to take care of this primary responsibility. In Indiana, we have come up with a situation where you have had these transshippers who are out of small communities, have no labor costs, have small operations, and have all the brands. In the big cities, the brewers had interbrand competition. In our particular city, we have got five major distributors, and they have five different brands of beer, and they have always been very competitive with each other. For instance, draft beer is not now being transshipped, because it is not profitable, and it is a big service item. Now, the man from the FTC said there would be no competition if you had exclusive territories. We, in effect, have the city of Indianapolis for draft beer, and yet we have intense competition. When I got into the business in 1975, the price of draft beer was $28.50 a barrel. Now we are selling it as cheap as $27.50 a barrel, mainly because we have this intense brand competition between Miller, Budd, Stroh's, Pabst, and Budweiser, and everybody is constantly fighting for the taps. So you have got good competition between interbrands, and you are having people serviced, and they are doing all the things that they are supposed to be doing. But in this case, we are all dealing from the same place. We are dealing in a fair competition, where we are all dealing from the same deck.

Now, in Indiana, these people that are in these small communities, at one time, because the small communities could not afford a number of distributors in a particular county, they gave them all the brands of beer. Well, these people, with all the brands of beer, come into our particular territory, come to a big retailer, and give him a discount based on 5 or 6 different brands of beer, in some cases, 20 brands of beer. Therefore, they can give a discount on 100 cases and give him a quantity that he can use. We can only come in with one particular brand of beer to try to match this. Now, in our case, our 50-case price is approximately the same as Beerco's 1,500-case price. And we are giving them 50 cases of Stroh's against 1,500 cases of all the rest of the beers, and yet, they will not take our beer, because one of the distributors, a Budweiser distributor in our area, will not discount, so consequently, whatever we do, no matter how much we reduce the price, we cannot get the beer. The other thing they do is "cherry-pick." They take all the big accounts, leave all the nonprofitable accounts for us to service, and we just cannot exist. So consequently, I think transshipping and the failure to have a territory prevents you from properly marketing your beer in your area, properly doing what you are supposed to do for the brewers. The brewers' hands have been tied by lawsuits in these matters, and I think we need this bill to preserve fair competition and to give the people that have a particular brand of beer in a community the satisfaction and the knowledge to know that he can go out and spend money to promote that beer, and perhaps that beer will be No. 1. Now, in our case, Stroh's was No. 1 for 7 years, even though Budweiser was the No. 1 beer in the country, and it was only the No. 1 beer because we spend like 50 to 60 cents a case promoting it, and promoting it in our own area. Now we are not doing anything. All of a sudden, Stroh's has gone to a No. 5 position, and they are just not competitive with the Miller and the Budweiser, because you are strictly depending on the tube; there is no more local promotion on the wholesale level.

That is all I have to say.

[The following was received for the record:]

PREPARED STATEMENT OF RAYMOND J. JUSTAK, VICE PRESIDENT, TODD & JUSTAK, ON BEHALF OF THE BEER DISTRIBUTORS OF INDIANA, INC.

Once upon a time there were seven beer wholesalers in Indianapolis, Indiana. They all made enough money to support two families (one Republican, one Democrat), they had fleets of overland trucks to haul beer to and from the breweries, fleets of city trucks to deliver beer, one or two party trucks, and large warehouses with adequate inventories. They paid high wages, contributed to pension funds, and paid top dollar for medical and other fringes. They contributed equally to both political parties, supported the local symphony and other cultural events, paid for broadcasting baseball games, and donated to high school yearbooks (always anonymously, because beer and high schools don't go together—at least not in those days.) The year? 1972.

Ten years pass. There are now five beer distributors left in Indianapolis, with two ready to merge or go under. One for sale cheap, one which subsidizes its operation from the earnings of another business. None has made money for five years. Like the hibernating bear, they have been living off their own fat. Now they are down to the skeletons.

Ten years age each of these distributors had one major brand and several smaller brands. They serviced about 1,200 accounts at least once a week. They competed fiercely inter-brand. They were careful not to talk prices with each other for fear of violating antitrust laws. They sold to every retailer, no matter how small, at the same price, as they were required to do by law, arranged displays, put up point-of-sale advertising, handled claims, rotated stocks—in short, merchandised and serviced their accounts as the breweries wanted them to. They employed over 550 people.

Today, 400 of those 550 have been laid off; union drivers are working as warehousemen, office staffs have been cut to the bone. No more advertising. No charitable contributions. Overall—in a market which has increased dramatically in sales over the ten-year period, they are down 2½ million cases from their 1970s sales peak.

As every wholesaler knows, there is a break-even point in beer sales. Below it you lose money; everything over and above it is profit. If the per case profit goes down, it takes more cases to reach and exceed the break-even point. The loss of these 2½ million cases took Indianapolis wholesalers well below the break-even point.

Where did these cases go, and the additional one million-plus cases sold in the Indianapolis metropolitan area last year which represented increased consumption?

They went to 15 transshipping wholesalers—in large part to a wholesaler from Hartford City, Indiana, who used to sell 80,000 cases in its area of primary responsibility and now sells 2½ million cases, all financed by Uncle Sam with an SBA loan, and by hidden principals.

How did it happen?

In 1935, when the state passed a comprehensive act regulating the sale and use of alcoholic beverages. over 37 of Indiana's 92 counties had voted "dry." The provisions of the act were designed to "promote temperance" by limiting and restricting the sale and use of alcoholic beverages, and "to prohibit forever the open saloon," which had been so ubiquitous and so offensive in pre-Prohibition days. Another purpose was to keep the criminal element out of the industry (control by Chicago gangsters had been a problem during Prohibition).

Politicians also saw the act as a way to raise revenue (through excise taxes and license fees) and to dispense political patronage (through licenses). They set up a three-tier distribution system (from brewer to wholesaler to retailer) and regulated and licensed every phase of the industry, with an Alcoholic Beverage Commission authorized to make the rules and administer the law.

From 1935–1945 Democrats were in control of the state and of the beer business. In 1945 Republicans took over the governor's mansion and the state legislature passed the "Ripper Bill," which revoked every alcoholic beverage permit in the state. All Democrats would have lost their wholesale licenses at that time except for World War II which made starting a new business difficult, so some Democrats managed to stay in business by taking in Republican partners. When the Democrats came back four years later, they profited by this experience and established the famous "marriage plan"—to get a new license or renew an old one Republicans had to "marry" Democrats and vice versa, so there was one of each faith in the business.

From 1956 through 1972 the industry was stable and prospered, as the governor's office shifted back and forth regularly between the two political parties.

In 1967 came the first intimation of trouble. The United States Supreme Court decided the Schwinn case, which held that exclusive territory agreements were per se unreasonable restraints of trade under the antitrust laws. Brewers, who had until then operated under exclusive territory franchises, went to what they called "areas of primary responsibility." Wholesalers were not restricted to their primary areas but they tended to respect them. In Indiana, there were 92 counties and about 220 wholesalers. In Indianapolis and other metropolitan areas they were single brand wholesalers, with county-wide responsibility; in counties with smaller cities there were two or three multi-brand wholesalers; and in the areas with small populations and long distances to cover one wholesaler might have all the brands.

Everything about the industry was regulated, remember, because the object was to promote temperance. And advertising was one of those regulated things. While the act specifically allowed newspaper advertising, the ABC had power to fix the terms and conditions, and it did not permit price advertising of brands. Also, at that time in the liquor portion of the industry, there were uniform price mark-ups and uniform fair-trade retail prices, and if prices were uniform fair-trade retail prices, and if prices were unform, there was very little point in advertising.

The two Indianapolis papers, both owned by the same family, sharing the same building and a common advertising department, did not like this situation at all and set out to change it. In early 1972 they ran a series of articles attacking the ABC and fairtrade liquor prices and price mark-ups. Eventually they got their way. Liquor price mark-ups were abolished, liquor prices were advertised, and liquor advertising became an enormous source of revenue to the two newspapers. They then set out to get beer advertising also.

After the Indianapolis Star set the course, several ambitious young lawyers filed antitrust suits against the liquor industry and the ABC, challenging the price markup system. They won. Then the newspapers, tasting success, directed their attack against the beer business, and specifically against beer wholesalers. Shortly thereafter, another antitrust suit was filed, by some of the same lawyers, this time naming the brewers and about 20 wholesalers as defendants.

In the meantime, in the northern part of the state, retailers began hauling beer from the dock of a wholesaler in Winamac, Indiana, and the Indianapolis papers heralded this as a great victory for consumers everywhere. Another wholesaler began selling at dock, and then another. Law suits were filed on behalf of the wholesale industry after the ABC refused to act to halt the practice (called both "dock-sales" and "retailer hauling") and after the governor refused to intervene.

Beer wholesalers now found themselves beset on all sides, but they were not astute enough to see the web of conspiracy being woven. The brewers might have stopped the whole process cold by taking action at this time, but they were not sufficiently alarmed on the one hand, and perhaps a bit timid on the other: the national climate was anti-business, and there were the Schwinn case and the antitrust suit to consider. They could not have stopped selling beer to the renegade wholesalers, or discriminated against them as to price, because the ABC was always alert to enforce the rules against the brewers and legitimate wholesalers; but there were actions they could have taken which might have been effective. Instead, they did nothing, and by their default have given up control over the distribution system in Indiana.

What happened next was like a few frames taken from a reel of a Laurel & Hardy comedy: there was a bombing in Winamac, Indiana, where the retail hauling had started. It did $300 worth of damage, and there was no evidence at all of any participation by anyone outside of Winamac. But the Indianapolis newspapers acted as if this were the prelude to World War III. Two Congressmen who were running for re-election called for an investigation, and the machinery of the Justice Department was started up, to grind slowly to a halt only years later with not one indictment returned against any Indiana wholesaler. But it was estimated that this little $300 smoke bomb cost legitimate distributors in Indiana over half a million dollars, and the taxpayers God knows how much.

Governor Otis Bowen had said before he went into office that he would abide by the "will" of the legislature with regard to the alcoholic beverage business, but this changed: in 1976 when the legislature expressed its will by passing an act outlawing retailer hauling (70-25 in the House; 26-21 in the Senate), the governor responded by vetoing the measure. When the bill came up on an override vote the following year, the House voted to override, but the Senate was tied, and Lieutenant-Governor Orr cast the deciding vote against the measure.

The large supermarkets wanted to buy their beer from the breweries direct at wholesale prices, and treat it as casually as any other commodity on their shelves. The chain package stores wanted to buy beer in large quantities at discount prices (which had never been allowed), store it in their own warehouses, and run specials to eliminate small competitors. The drug stores wanted to become package stores selling drugs. The large independent retailers wanted to buy cheap and sell at whatever prices the market would bear, and so did the tavern owners.

None of these goals could be pursued under the 1935 Act, which had been designed to "limit and restrict" the sale and use of alcoholic beverages, not to make them cheap and available. All the rules that had been developed in 40 years of experience prohibited what these people wanted: unrestricted advertising; quantity discounts; retailer warehousing; co-op advertising; retail hauling; co-op purchasing and warehousing; any hauling or selling outside of the county in which the seller's business was located; and any price discrimination by the brewers or wholesalers.

If they had gone to the legislature with bills to abolish the ABC or to accomplish these specific goals, they would have been defeated. So they set out to do indirectly what it was not possible to accomplish in the full glare of the legislative process, even with the blessing of the Indianapolis Star.

When the Beer Distributors of Indiana (BDI) requested a ruling as to the legality of dock sales, the ABC procrastinated for over two years. The Federal Court intervened, mandating the ABC to fulfill its administrative function. Reluctantly, facing the threat of contempt proceedings, the ABC did finally act, and issued a ruling saying that the practice was legal (it had, after all, only been considered illegal for 40 years!)

The wholesalers now had something they thought they could take to court. They did, and the trial court, in a carefully reasoned opinion, said the ABC was wrong. But the Indiana Appellate Court overturned the trial judge, not deciding the merits of the case, but on the old familiar judicial throwaway, "failure to exhaust administrative remedies" (the obverse side of this coin is "the law will not require the performance of useless acts," and the judge selects whichever doctrine fits the way he wants to decide the issue).

But all this legal maneuvering (and these were only two of many cases) took several years, and in the meantime the point became moot. The few northern Indiana wholesalers who had been selling at dock now decided to haul the beer into the metropolitan areas themselves. When the renegade wholesalers discontinued dock sales in favor of wholesaler hauling (also known as "transshipping"), the ABC could find nothing in the law which prohibited this practice, either.

This is what happened and is still happening: a small town wholesaler with all the brands hires a gypsy trucker, or uses his own semi, and hauls beer to Indianapolis or Hammond where he dumps it at the customer's place of business in large quantities.

Because he has all the brands, he can not only sell "your" brand at a lower price (due to lower costs), he can mix and match your brands and packages. He cherry-picks the large accounts, pre-sells your other good accounts for his next trip down, and skips town.

The local man is left to pay the real estate and license taxes and buy the tickets to the Policeman's Ball. He is also expected to pick up the old beer if the retailer fails to sell all of his large order before it goes stale; to advertise the brewer's products; to settle claims and trouble shoot.

He has to send out clean trucks and uniformed drivers. He must continue to pay union wages at the big city level, with fringes that were tacked on at a time when he was making money, and to service all the 10-case-and-under accounts which make up 50 percent of the market but are not profitable. These customers, incidentally, will not be happy if they have to pay more for their beer than the transshippers are charging for 500-case drops. In some cases the transshippers are even bolder, and have the beer delivered direct from the brewery to the customer by commercial carrier, taking an overwrite on the sale.

A legitimate wholesaler who sees a hauler from a nearby county getting fat stealing his business on the way to Indianapolis or Bloomington or Evansville, ultimately comes to the conclusion that he can no longer be expected to hold the line. The situation has become so ludicrous in Indiana that transshippers are cherry-picking transshippers, and one wonders if anyone is making money. Meanwhile, with every new lawsuit, every new appeal to the ABC, every attempt at curative legislation, the Indianapolis newspapers wave the flag and hail the haulers as exponents and defenders of "free enterprise."

There was a glimmer of hope in 1977 when the Supreme Court, after ten years, reversed itself and returned to the pre-Schwinn rule that an exclusive territory was bad only if it constituted an unreasonable restraint of trade. By then, however, the proponents of an unregulated alcoholic beverage industry in Indiana had now gotten a firm hold. Liquor and beer were extremely cheap and very available. The newspapers had pages and pages of advertising each week, and salved their consciences by periodic diatribes against the perils of drunkenness and sales to minors. There were now 130 wholesalers in the state instead of 210, with an accelerating rate of attrition each year. Alcoholism had increased, particularly in the under-30s group, and accidents and deaths due to drunken operating were substantially higher, but this did not count when weighed against the Gold Dust Twins, "free enterprise" and "consumerism."

But now the Schwinn case was reversed and the brewers might go back to exclusive territories. Something had to be done to prevent this.

The ABC came up with the perfect solution—Rule 28.

Rule 28 provides that it is illegal for brewers to enter into exclusive territory agreements with their wholesalers. The beauty of the rule was that it was entirely original—no other state had such a provision. It wasn't specifically authorized by any statutory language, but this didn't make any difference. The chairman of the ABC said he didn't agree with the rule of strict construction applied by the courts anyway; and the rule became "law."

In the meantime, the General Assembly created an alcoholic beverage study committee, specifically charged, among other things, with reviewing the beer distribution system and making recommendations. The committee was composed of both legislators and public members. The public members were attorneys and lobbyists from different segments of the industry, but the public member selected to represent the interests of the wholesalers was—you guessed it, a transshipper! Even with the composition of the committee stacked against the wholesalers, the final recommendation of the committee was that legislation be adopted to prohibit the ABC from interfering in beer distribution agreements.

And then came, not a change of administration, but a new governor and a wholly new ABC, and the hope which springs eternal did spring again in the breasts of the wholesalers. Robert E. Orr had been a businessman and, for a time, associated with Sterling Brewery in Evansville. He knew the industry. The wholesalers, therefore, had every reason to believe he would want to stop what they could only regard as political persecution and bring order out of chaos.

In November 1981, it appeared as though their hopes might be justified. The new commission did put the repeal of Rule 28 on its agenda. It was set for hearing on March 23, 1982.

As the hearing date drew near, there was a great hue and cry in the media, but absolutely no public interest in the matter. The only calls, letters and telegrams to the governor's office were from beer wholesalers, their insurance men, their bankers, their attorneys, and their loyal retailers (bless 'em all), all pleading for repeal. The television stations, following the lead of the newspapers, made their little editorial statements in favor of Rule 28. With no understanding of the issues involved they echoed the newspapers, not realizing that in this instance the press was serving itself and not the public.

The hearing was held and the arguments heard. The commission gave parties 30 days in which to file briefs, and indicated it would take as much time as necessary thereafter to study them. Then on April 21st, two days before the expiration of the time for filing briefs, the ABC called the media to announce that a decision would be rendered that afternoon at its meeting, and that it would be 4-0 in favor of retaining Rule 28. It appears that someone may have called in his political chips.

So what is the situation in Indiana today? Even if the Malt Beverage Interbrand Competition Act is passed, as we all sincerely hope it will be (neither of the two Indiana senators has indicated he will vote for it, though) it is too late to save the three-tier distribution system in Indiana. Only drastic retributive action by the brewers can have any effect at this late date, and so far Anheuser-Busch is the only brewer who has shown any determination to run its own show.

To survive now, Indianapolis wholesale houses must merge to become multi-brand houses, or must become master distributors with large territories. The small retailer is probably doomed; the small wholesaler is inevitably doomed; wholesalers, large and small, will continue to go under; and the 210 profitable family businesses of the past will condense into perhaps 20 giant wholesalers covering the state.

Bootlegging into the state will continue for a while, and beer will continue to be cheaper than soft drinks, as it is now in many areas, until the survivors among the wholesalers have divided up the market between them. Then prices will go up again to realistic levels.

The current Alcoholic Beverage Commission, which started out to administer the law with so much enthusiasm, has been publicly embarrased and effectively neutralized, and will find it difficult to make any hard decisions in the future.

The supermarkets and drug stores will continue to push for the right to sell cold beer, and ultimately, the right to sell hard liquor off the grocery shelf; and the package stores will then find their operations increasingly less profitable.

Small taverns will be driven out of business. Because of the ineffectiveness of the ABC, the large 1,500-2,000 capacity bars will provide a cover to sell stale tap beer to young people, and they will become not much different than the saloons which the men who drafted the 1935 Act sought to outlaw.

The supermarkets will push their cheap "no brand name" beers, and will sell name brands below cost as "loss leaders," which of course does nothing to "limit and restrict the use of alcoholic beverages."

We can only hope that the organized criminal element does not move back in with an infusion of capital for dying wholesalers as a preliminary to taking over, in which case we shall have come full circle.

One wonders if these are the consequences which the politicians of Indiana foresaw and intended, and continue to bless today?

[Letter to the editor of the Indianapolis News, in response to a March 24, 1982, article in that newspaper]

NOT BARONS

To the Editor of the News

In response to your editorial "Bellying up to the ABC," we are the owners of a small town neighborhood tavern and are in favor of not what you term the "beer baron bill," but what we like to call "hometown service."

We do not wish to buy our beer outside of the county in which we live. We do not make any purchases for our business outside of our county, unless it is unavailable locally. Our local distributor, who has been in business for over 40 years, has not only been good to the local taverns and liquor stores, but has had a deep interest in our community.

How can you write such editorials and tell us it is a reaffirmation of free enterprise? If our local distributor is run out of business, because of "new wholesalers" outside of our county, we will be very hard pressed for good service. We know our service is good now, but how do we know our service will stay high in quality, when our beer will have to come over 60 miles?

BETH BUGG.

Marion.

National Beer Wholesalers' Association of America, Inc.

Executive Offices
Suite 505
5205 Leesburg Pike
Falls Church, Virginia 22041
703/578-4300

News Release

For Release: Noon, August 5, 1982
For Information: Frank McNeirney,
NBWA Director of Communications

WASHINGTON, DC, August 5, 1982--Two Indiana beer distributors urged Congress today to enact legislation protecting the right of brewers and beer wholesalers to maintain exclusive territorial agreements in areas where substantial competition exists among brands.

Matthew R. Dee of United Beverage Co. of South Bend Inc. and Raymond J. Justak of Todd & Justak, Indianapolis, testified at a hearing of the Senate Judiciary Committee in favor of the Malt Beverage Interbrand Competition Act (S. 1215). This bill, co-sponsored by 66 senators, would confirm that such exclusive agreements do not violate federal antitrust laws.

An identical bill, H.R. 3269, has been co-sponsored by 285 members of the House of Representatives.

Indiana beer distributors have been especially hurt by the absence of such a law, Dee and Justak noted, since the Alcoholic Beverage Commission rules of that state were changed several years ago to prohibit territorial agreements. This, they said, encouraged the growth of "transshipping," a practice whereby a distributor sells bulk quantities of beer to retailers--generally large supermarkets, chain package stores or similar outlets--outside his designated area.

Transshippers who invade established wholesalers' territories usually can undersell them, Dee and Justak pointed out, not only as a result of large volume shipments, but also because the established firms must continue to honor brewery contracts requiring them to service all accounts in their designated markets and to provide costly promotional and advertising services as well. Transshippers have no such responsibilities outside their originally designated territory.

"We're in a no man's land between free enterprise and total regulation," Dee told the Committee. Under the 21st Amendment, he explained, each State has the power to rigidly specify how, when, where and to whom beer can be distributed and sold. "This is not free enterprise in a true sense," he argued.

"Yet the lack of exclusive territories means that transshippers are free--free to go after only the biggest, most profitable accounts, leaving the smaller, less profitable ones to the established wholesalers," he added. "We call this cherry-picking."

Since the advent of transshipping in Indiana, Justak informed the Committee members, the number of beer wholesalers in the state has dropped from more than 200 to approximately 150, resulting in the loss of hundreds of jobs. Few if any of these jobs have been absorbed by transshippers, whose operations are characterized by truckload quantities and minimal service.

Of the 550 people employed ten years ago by beer wholesalers in Indianapolis alone, Justak reported, 400 have been let go. Were transshipping to affect the entire US beer wholesaling industry to the same extent, he warned, more than 50,000 jobs could be lost nationwide.

Both Dee and Justak emphasized that the bill would by no means mandate exclusive territories by requiring brewers and wholesalers to enter into territorial pacts. It says only that if substantial and effective interbrand competition exists in an area, then such agreements are not prohibited by federal law, they explained.

In earlier testimony at Senate and House hearings on the bill, other spokesmen for the National Beer Wholesalers' Association said its passage was needed to clarify the rights of States to regulate the distribution and sale of malt beverages under the 21st Amendment.

By confirming the lawfulness of territorial agreements, they noted, the proposed Act would lessen the possibility of needless litigation, the costs of which would ultimately be borne by consumers in the form of increased prices.

#

Sampling of Retail Prices
Six-Packs of Beer Sold
In Indiana
22 June 1982

DC-
AB - 250
LTG - 281

DC-
$2.44
[illegible]
Bud-[illegible]

CITY	BRAND	LARGE PACKAGE STORE	SMALL PACKAGE STORE	CHAIN STORE
Indianapolis	Budweiser	$ 2.59	$ 3.00	$ 1.99
	Miller Lite	2.59	3.00	1.99
	Pabst	2.59	3.00	1.99
	Strohs	2.59 2.58	3.00 3.00	1.99 1.94
	Schlitz	2.49	3.00	1.85
	Old Style	2.49	3.00	1.85
	Blatz	2.59	3.00	1.99
Evansville	Budweiser	2.05	2.31	1.99
	Miller Lite	2.12	2.31	2.03
	Pabst	1.97 2.10	2.26 2.29	1.92 2.[illegible]
	Strohs	2.09	2.31	2.04
	Schlitz	2.13	2.31	2.02
Terre Haute	Budweiser	2.80	3.10	2.45
	Miller Lite	2.80	3.10	2.45
	Pabst	2.70 2.80	3.10 3.10	2.35 2.42
	Strohs	2.80	3.10	2.45
	Schlitz	2.80	3.10	2.45
Bloomington	Budweiser	2.75	2.75	2.65
	Miller Lite	2.75	2.75	2.65
	Pabst	2.60 2.75	2.60 2[illegible]	2.60 2.42
	Strohs	2.75	2.75	2.65
	Schlitz	2.75	2.75	2.65
South Bend	Budweiser	2.25	2.19	2.19
	Miller Lite	2.25 2.25	2.19	2.25
	Pabst	2.10	2.19 2.10	1.99 2.16
	Strohs	2.25	2.19	2.19
	Schlitz	1.92	2.19	1.99

Sampling of Retail Beer Prices In Indiana (Six-Packs)

22 June 1982

BRAND	CITY	LARGE PACKAGE STORE	SMALL PACKAGE STORE	CHAIN STORE
Budweiser	Indianapolis	$ 2.59	$ 3.00	$ 1.99
	Evansville	2.05	2.31	1.99
	Terre Haute	2.80	3.10	2.45
	Bloomington	2.75	2.75	2.65
	South Bend	2.25	2.19	2.19
Miller Lite	Indianapolis	2.59	3.00	1.99
	Evansville	2.12	2.31	2.03
	Terre Haute	2.80	3.10	2.45
	Bloomington	2.75	2.75	2.65
	South Bend	2.25	2.19	2.25
Pabst	Indianapolis	2.59	3.00	1.99
	Evansville	1.97	2.26	1.92
	Terre Haute	2.70	3.10	2.35
	Bloomington	2.60	2.60	2.50
	South Bend	2.10	2.19	1.99
Strons	Indianapolis	2.59	3.00	1.99
	Evansville	2.09	2.31	2.04
	Terre Haute	2.80	3.10	2.45
	Bloomington	2.75	2.75	2.65
	South Bend	2.25	2.19	2.19
Schlitz	Indianapolis	2.49	3.00	1.85
	Evansville	2.13	2.31	2.02
	Terre Haute	2.80	3.10	2.45
	Bloomington	2.75	2.75	2.65
	South Bend	1.97	2.19	1.99
Old Style	Indianapolis	2.49	3.00	1.85
Blatz	Indianapolis	2.59	3.00	1.99

The CHAIRMAN. We will please hear from you now, Mr. Dee.

Mr. DEE. Thank you, Mr. Chairman.

My name is Matthew Dee, and I am the president of a small beer wholesalership in South Bend, Ind. I have been active in the company since 1959, although the business has been in the family since 1936. Our business has been in the community since 1932, and we feel that we are a viable part of our local community and economy for some 50 years.

I basically would like to make four points in regard to testimony that has been received already by opponents to the bill: basically, the advantages of transshipping; jobs; the supposed price advantage to the consumer, and the rule of reason that the Justice Department has used.

In June, Mr. Quinn, representing opponents to the bill, said that transshipping is just another word for competition. Well, that may be true. But they come into the market and only "cherry-pick," as Mr. Justak has said, calling on only high-volume accounts. They say it is an innovative method of distributing beer. Actually, they are doing nothing different than gypsies did years ago. They give nothing to the community, they contribute nothing to the tax base or to the local economy. They just take; they are not part of the community. They are basically raping the community in which I live under the guise of consumerism.

Two of the very large retailers in my community, two liquor chains who have been stressing the advantages to the consumer, are both presently operating under the protection of the Federal Bankruptcy Act under chapter 11. Mr. Quinn stated in June that there was no job loss in Indiana due to the transshipping. Baloney. In South Bend alone, 70 percent of the jobs related to the beer industry have been lost since 1978 and have not been replaced.

Price to the consumer. I enjoyed Ms. Fox's description of my business from the safety of her classroom. I invite her to join me in Indiana to see what the real world is like.

We did a pricing survey in Indiana and also in the local area here in Washington and Virginia and the surrounding area. We took Budweiser, Miller Lite, Pabst, Stroh's, Schlitz, Old Style, and Blatz. We did the survey in the cities of Indianapolis, Evansville, Terre Haute, Bloomington, and South Bend. We did it in three different types of accounts—large package stores, small package stores, and chain stores. We did the same thing here in Washington, and I did it personally while riding around in a taxicab.

We found, unlike what is being said, that transshipping causes lower prices to the consumer, that in the city of Indianapolis, the average price in the large package store for Budweiser, Miller Lite, Pabst, Stroh's, Schlitz, Old Style, and Blatz, is $2.58, with the low price being $2.49 and the high price being $2.59. In Washington, D.C., you can buy that same six-pack of beer for $2.59. The State tax in Indiana is approximately 25 cents per case; in Washington, D.C., the tax is 19 cents, while in Virginia, the State tax on that same package is 65 cents per case. So the tax really does not come into effect.

In the small package store, we found in Washington, D.C., it was $2.81 for a six-pack of Miller Lite, while in Indianapolis, the price for that same six-pack of Miller Lite was $3. In Terre Haute, it was $3.10, and in Bloomington, it was $2.69.

Mr. Chairman, I have made copies of this, and have already submitted it for the record.

So the pricing situation really is not a valid argument, in my opinion.

The last thing, which is the cost of litigation and the so-called rule of reason that Mr. Winslow has brought up. Listening to Mr. Winslow representing the Justice Department, I find his logic dealing with the applied rule of reason, in cases dealing with antitrust litigation, impractical in this particular industry. In practice, the rule of reason is extremely expensive to argue in court. I will enclose as part of my testimony a copy of a lawsuit filed in 1977 against beer wholesalers in the State of Indiana. The plaintiffs are a large drugstore chain and the primary transshipper in Indiana. The lawsuit is claiming treble damages of $175 million, under the Sherman Act, and was filed after the Justice Department, operating out of Chicago, had completed an investigation of the same charges in 1976, finding no basis for the charges. Since the inception of the lawsuit in 1977, beer wholesalers in Indiana have spent in excess of $300,000 defending themselves in this lawsuit. This has included answering four sets of interrogatories, testifying orally to other questions, and attempting to have the case taken to trial. I, personally, have spent over $23,000 for my defense counsel. At this writing, no trial date has been set definitely, although a pretrial hearing has been set for October. Bear in mind that this is now 5 years after the suit has been filed. For 5 years, 135 small, independent businessmen have been waiting and paying for a trial which will prove them innocent. I ask you, is this what you and the Justice Department would call proper application of the antitrust laws and the rules of reason?

Congressmen have questioned the need for this legislation during the hearing. I would ask them that a state of emergency exists in this industry at this time; failure to pass this bill will allow the continual abuse of antitrust laws to the detriment of those who cannot afford to defend themselves. The real reason is whether you will continue to allow well-financed groups in the grocery and drugstore industry to file unfounded lawsuits of this nature, forcing small businessmen like myself to either give up, or go broke trying.

Thank you.

[The following was received for the record.]

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF INDIANA
FORT WAYNE DIVISION

RECEIVED
JAN 15 1979
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Harman, Carey & Murray

ARTH MAIN STREET DRUGS, INC.,
ARTH DRUGS, INC.,
ARTH SOUTH FOURTH DRUGS, INC.,
ARTH STATE STREET DRUGS, INC.,
ANTFAHL, INC.,
BAR BARRY LIQUOR STORE, INC.,
OTIS BURKETT, INC.,
ANTHONY CARRARA,
THE COUNTY SEAT HOTEL, RESTAURANT
AND BAR, INC.,
CSA, INC.,
DeLOCK'S #1, INC.,
DeLOCK'S #3, INC.,
DeLOCK'S #6, INC.,
DeLOCK'S #11, INC.,
DeLOCK'S #14, INC.,
ED'S PALMER HOUSE, INC.,
CLARENCE W. EPLEY, JR.,
MARY EVANS,
EARL FULLER,
C. R. HADDOCK,
EDDIE C. HARDIN,
R. L. HATCHER, INC.,
JOHN W. JANES, III,
JAMES M. HACKLEMAN,
J & J THRIFTWAY SUPERMARKETS, INC.,
KARY-OUT CORP.,
EDMUND R. LELITO,
JOHN M. LOFTUS,
MEYERS VENTURES, INC.,
J & M MOORE, INC.,
NICHOLS' THRIFTWAY SUPERMARKET, INC.,
NORTHCREST LIQUOR STORE, INC.,
O'HANLON, INC.,
ALEX PAPP
THRIFTWAY QUALITY FOODS, INC.,
21ST AMENDMENT, INC.,
WALKERTON STAR CAFE, INC., and
WESTVILLE LIQUORS, INC.,

Plaintiffs,

vs.

CAUSE NO. F-77-73

BEER DISTRIBUTORS OF INDIANA, INC.,
AALCO DISTRIBUTING CO., INC.,
RICHARD D. JONES,
A-1 BEVERAGE CO., INC.,
CLYDE FISCUS,
A. B. BEVERAGE CO., INC.,
MARIE P. BROWN,
ACE BEVERAGE CO., INC.,
EDWIN RATCLIFFE,
ACME BEVERAGE, INC.,
RICHARD K. BRINKER,
ADAMS DISTRIBUTING CO., INC.,
W. A. KLEPPER,

EXHIBIT C

ALLEN PRODUCTS, INC.,)
SID HUTNER)
ANGOLA DISTRIBUTORS, INC.,)
EDWARD J. WILLIAMS,)
B & G DISTRIBUTOR CO., INC.,)
PAUL O. GORHAM,)
BARCO BEVERAGE CORP.,)
ROBERT V. WELMER,)
BARTHOLOMEW COUNTY BEVERAGE CO., INC.,)
FRANCIS M. OVERSTREET)
BEST BEERS OF BLOOMINGTON, INC.,)
ROBERT A. HAAK,)
BETTER BRANDS, INC.,)
TOM BRODSKY,)
BILL'S BEVERAGE, INC.,)
LOUANNA YOUNG,)
BILTZ BEER DISTRIBUTORS,)
IMOGENE E. BILTZ,)
BLUE RIVER PRODUCTS, INC.,)
WAYNE KELLAMS,)
BOONE BEVERAGES, INC.,)
CURTIS H. SELBY,)
BRENTLINGER DIST. CO., INC.,)
RICHARD C. BRENTLINGER,)
BROADWAY BEVERAGE CO., INC.,)
GEORGE W. SASSER,)
BROWN BEVERAGES, INC.,)
LOWELL J. BROWN,)
BROWN COUNTY BEVERAGE,)
ARTHUR WOLPERT,)
BRUMM DISTRIBUTING COMPANY, INC.,)
DWAIN W. BRUMM,)
B-F BEVERAGE CO., INC.,)
WILLIS H. MARLOWE,)
C & J BEVERAGE CO., INC.,)
BERNARD J. MONTGOMERY,)
CALUMET BREWERIES, INC.,)
GEORGE E. KIERNAN,)
CAVANAUGH MALT BEVERAGE, INC.,)
MRS. GEORGE CAVANAUGH,)
CENTRAL BEVERAGE CO., INC.,)
W. R. SCOTT,)
CENTRAL BEVERAGE CO., INC.)
EUGENE C. TURNER,)
CENTRAL DISTRIBUTING CO., INC.,
JOSEPH BULEY,)
CENTRAL DISTRIBUTOR OF MARION, INC.,)
SAM J. CONIGLIO)
CITY BEVERAGE, INC.,)
MICHAEL T. FISHER,)
CITY BEVERAGE OF LOGANSPORT, INC.,)
JOHN T. COTNER,)
CLARK COUNTY BEVERAGE CO., INC.,)
FLOYD THROCKMORTON,)
CLARK COUNTY DISTRIBUTING CO., INC.,)
IRA B. MCKINLEY,)
COLUMBIA CITY BEVERAGE CO.,)
HENRY A. SIEVERS,)
HELEN I. SIEVERS,)
COLUMBUS BEVERAGE, INC.,)
ERMA R. COLLIER,)
CONNERSVILLE CITY BEVERAGE, INC.,)

CLOYCE BLUE,)
COUDEN DISTRIBUTORS, INC.,)
JOSEPH R. COUDEN,)
C'VILLE BEVERAGE CO., INC.,)
JAMES STEPHENS,)
D & B BEVERAGE, INC.,)
HARCOURT SCALES,)
D'ANDREA DISTRIBUTING CO., INC.,)
RESTO D'ANDREA,)
BEN DAULTON DISTRIBUTING CO., INC.,)
BEN DAULTON,)
DECATUR BEVERAGE CO., INC.,)
WILLIAM E. CRISTER,)
DEKALB DISTRIBUTING CO., INC.,)
JOHN N. GRIMM,)
DELAWARE BEER CO.,)
ROBERT E. HEATH,)
DERR'S, INC.,)
CHARLES A. DERR,)
DEVER DISTRIBUTING CO., INC.,)
LUKEN E. DEVER,)
DUBOIS COUNTY BEVERAGE CO., INC.,)
MARIE E. GRAMELSPACHER,)
ELKHART COUNTY BEVERAGE CO., INC.,)
DOMINIC IEMMA,)
ELKHART DISTRIBUTING CORPORATION,)
C. N. ELDRIDGE,)
DICK ELLIOTT DISTRIBUTORS, INC.,)
FRANK CALLIPO,)
EXCEL DISTRIBUTING CORP.,)
THOMAS H. WOLFRUM, I,)
FARBER DISTRIBUTING CO., INC.,)
LEONARD FARBER,)
FAYETTE REFRESHMENT CORP.,)
HELEN MCKENNA,)
FEDDER DISTRIBUTING, INC.,)
EDWARD M. HAGERTY,)
FLOYD COUNTY BEVERAGE, INC.,)
LORRAINE B. WARMOTH,)
FOCHT BEVERAGE CO., INC.,)
WILLIAM FOCHT, SR.,)
FOWLER BEVERAGE CO., INC.,)
B. B. OVERHOLSER,)
FRIENDLY BEVERAGES, INC.,)
JACK L. MCCORMICK,)
FULTON COUNTY BEVERAGE)
  DISTRIBUTORS, INC.,)
JUDY BURTON,)
G & K WHOLESALE BEVERAGE CO., INC.,)
WILLIAM B. JONES,)
GEM CITY BEVERAGE CO., INC.,)
WALLACE P. IRWIN,)
MICHAEL I. CURTS,)
GENERAL BEER DISTRIBUTORS, INC.,)
VICTOR GIANINNO,)
GENERAL BEVERAGE, INC.,)
ROBERT L. SIEBERT,)
GIBSON COUNTY DISTRIBUTING CO.,)
FRANK GREUBEL,)
ADOLPH GREUBEL,)
GOLD-HART DISTRIBUTING, INC.,)
RONALD J. MOLLAUN,)
GOODLAND DISTRIBUTORS, INC.,)
DALE E. STAYER,)

GRANT DISTRIBUTORS, INC.,)
R. P. KILEY, JR.,)
GREENE COUNTY DISTRIBUTING CO.,)
HERMAN ULAND,)
GREENFIELD BEVERAGE CO., INC.,)
JOSEPH T. DUFFY,)
JOHN L. KIRKPATRICK,)
H & K BEVERAGE CO., INC.,)
ALLEN CRAFT,)
HAMILTON COUNTY MALT BEVERAGE, INC.,)
REED M. MILLER,)
HENRY COUNTY BEVERAGE CO., INC)
JOHN D. YERGIN,)
W. F. HOLLAND DISTRIBUTORS, INC.,)
CHARLES E. HOLLAND,)
THE HOME BEVERAGES, INC.,)
HOOSIER BEVERAGE CO.,)
DONALD W. WARREN,)
INDEPENDENT BEER DISTRIBUTING)
CO., INC.,)
WILLIAM F. NEELY)
J & N BEVERAGES, INC.,)
MRS. GLENN NICKLESS,)
JASPER BEVERAGE CO., INC.,)
ROBERT HEDINGER,)
JAY COUNTY BEVERAGE, INC.,)
JAY MILLER,)
JEFFERSON COUNTY BEVERAGE CO., INC.,)
JOHN H. HOFFMAN,)
GEORGE LEININGER,)
JENNINGS BEVERAGE CO., INC.,)
DONALD B. MILLER,)
JOHNSON COUNTY BEVERAGE, INC.,)
ELIZABETH J. DUHAMELL,)
JUERLING BEVERAGE CORP.,)
VINCENT C. JUERLING,)
J. W. BEVERAGE CO., INC.,)
CHARLES WOOFENDALE,)
K & H DISTRIBUTING CO., INC.,)
ALEX KING, SR.,)
KENDALLVILLE DISTRIBUTORS CORP.,)
GERALD A. PARKER,)
KEYSTONE BEVERAGE CO., INC.,)
ROY V. CALKIN, JR.,)
KNOX COUNTY BEVERAGE CO., INC.,)
ALEX J. TOTH,)
KOSCIUSKO BEVERAGE CO., INC.,)
BETTY J. DUST,)
KUHN BEER DISTRIBUTORS, INC.,)
KARL J. KUHN,)
LAFAYETTE BEVERAGE DISTRIBUTORS, INC.,)
JAMES E. LAMB,)
LAKES BEVERAGE CO., INC.)
OF MONTICELLO)
JACK MACY,)
LAKE COUNTY BEVERAGE CORP.,)
SAM MALETTA,)
LAPORTE COUNTY BEVERAGE CO., INC.,)
ROBERT L. ROULE,)
LAWRENCE COUNTY BEVERAGE CO., INC.,)
CLARENCE J. DONOVAN,)
LESLIE-POWERS DISTRIBUTORS, INC.,)
HILDA D. LESLIE,)

LESTER BEVERAGES, INC.,)
E. MORTON LESTER,)
LINCOLN HILLS BEVERAGE CO., INC.,)
DAVID C. HAYWOOD,)
LINTON BEER SALES, INC.,)
FRANCIS D. BAKER,)
LIQUIDS, INC.,)
JOSEPH W. E. CHAMBERS, SR.,)
LITTLE BEVERAGE COMPANY,)
JAMES B. WALLACE,)
LOCAL BEERS, INC.,)
JAMES H. BRUGGENSCHMIDT,)
LOOGOOTEE-SHOALS BEVERAGE CO., INC.,)
W. A. FISHER,)
LOWRY WHOLESALE BEVERAGE, INC.,)
ROBERT L. LOWRY,)
ED J. LUTHER BEVERAGES, INC.,)
LAWRENCE C. LUTHER,)
MACE & SONS, INC.,)
GEORGE R. MACE,)
MACO BEVERAGE CORPORATION,)
THEODORE F. SMITH,)
MADISON DISTRIBUTING CO.,)
E. W. JOHNSON,)
MAGIC CITY BEVERAGE COMPANY, INC.,)
KENNETH L. SHIVELY,)
MARION DISTRIBUTING CO., INC.,)
JOSEPH E. BARTON,)
MARSHALL COUNTY BEVERAGE CO., INC.,)
RICHARD L. FLAGG,)
MARTIN COUNTY DISTRIBUTORS, INC.,)
EUGENE DUPPS,)
MICHIANA BEVERAGES, INC.,)
J. GEORGE KARRAS,)
MILLER BEVERAGE, INC.,)
JACK H. KRANER,)
MONARCH BEVERAGE CO., INC.,)
EDWIN T. FRENCH, JR.,)
MONTGOMERY COUNTY BEVERAGE CO., INC.,)
R. EDWARD DICKERSON,)
MONROE BEVERAGE CO., INC.,)
BENJAMIN M. SHERIDAN,)
MORGAN COUNTY BEVERAGE, INC.,)
HAROLD HAMMONS,)
MORRISON BEVERAGE, INC.,)
RICHARD MORRISON,)
LEO J. MURPHY CO., INC.,)
JERRY JOHNSON,)
NACHAND BEVERAGE COMPANY, INC.,)
EDWARD C. SCHULER,)
L. C. NADORFF & SON, INC.,)
LEO C. NADORFF, II,)
NOBLE COUNTY BEVERAGE CO., INC.,)
FREEMAN E. TYLER,)
NORRIS BEVERAGE, INC.,)
JOHN W. CLEVELAND,)
NORTH VERNON BEVERAGE CO., INC.,)
NELSON HORTON,)
OHIO VALLEY BEVERAGE CO., INC.,)
HARRY POELLMAN,)
OLD CAPITOL BEVERAGE CO., INC.,)
HOWARD D. DENBO,)

ORANGE COUNTY BEVERAGE CO., INC.,)
ROBERT E. WININGER,)
PATOKA VALLEY BEVERAGE CORP.,)
ALVIN C. RUXER,)
PFEIFFER DISTRIBUTING CO., INC.,)
ROBERT R. BENNETT,)
POCKET BEVERAGE COMPANY, INC.,)
LEE O. GODEKE,)
POLLARD & BURTON, INC.,)
CARL MELSON,)
POLSTER BEVERAGE CORPORATION,)
WILLIAM E. POLSTER,)
POSEY COUNTY BEVERAGE CO., INC.,)
ELMER F. FEHR)
PUTNAM BEVERAGES, INC.,)
ROBERT S. MICHAEL,)
QUALITY BEERS, INC.,)
BERNARD A. CRIMMINS,)
RED BRIGHT BEER DISTRIBUTING CO., INC.,)
ROBERT G. BRIGHT,)
RHOADS BEVERAGE CO., INC.,)
JOHN L. RHOADS,)
THE RIPLEY COUNTY BEVERAGE CO., INC.,)
WILLIAM R. GUTZWILLER,)
RIPLEY COUNTY WHOLESALERS, INC.,)
HARVEY SIEBERT,)
ROCKVILLE WHOLESALE CORPORATION,)
MAX WELCH,)
RUSH COUNTY BEVERAGE CO., INC.,)
JIM G. EMERSON,)
S & O BEVERAGE CORP.,)
LARRY JONES,)
SALEM BEVERAGE CO., INC.,)
ROBERT L. SHRUM,)
SCHEMBRE BEVERAGE CO., INC.,)
JOSEPH J. SCHEMBRE,)
SCOTT COUNTY BEVERAGE CO., INC.,)
DONALD JONES,)
SCOTT COUNTY DISTRIBUTING CO., INC.,)
WILLIAM H. JAMES,)
THE SHANNON CORPORATION,)
BRUCE WRIGHT,)
SHELCO BEVERAGE, INC.,)
PAUL LOCKRIDGE,)
SOUTHEASTERN BEVERAGES, INC.,)
ROBERT W. HASTINGS,)
SPENCER COUNTY BEVERAGE CO., INC.,)
MICHAEL A. ROHL,)
SPRINGER, INC.,)
BEN R. SPRINGER,)
STARKE COUNTY BEVERAGE CO., INC.,)
GENE A. CARYER,)
SULLIVAN COUNTY DISTRIBUTING, INC.,)
HAROLD E. FLEENER,)
SUNNYSIDE BEVERAGES, INC.,)
THOMAS W. DENNIG,)
TELL CITY BEVERAGE CO., INC.,)
CHARLES F. HERRMANN,)
THREE RIVERS BEVERAGE CO.,)
CHRIST M. ROUSSEFF,)

TODD & JUSTAK, INC.,)
THOMAS E. TODD,)
TOWN & COUNTRY BEVERAGE, INC.,)
LEON M. COLGROVE,)
TREE CITY BEVERAGE, INC.,)
EUGENE GARRETT,)
TRI-CITY BEVERAGE CO., INC.,)
FRANK K. FINNERAN,)
TRI-STATE BEVERAGE CO.,)
HUGH G. BEGGS,)
UNITED BEVERAGE CO. OF SOUTH BEND, INC.,)
MATTHEW R. DEE,)
VALLEY BEVERAGE CO.,)
GENE NICOLINI,)
VALPO BEVERAGES, INC.,)
BRUCE LEETZ,)
VANCO BEVERAGE, INC.,)
HENRY M. LARUE,)
VERMILLION BEVERAGE, INC.,)
ROBERT WALLACE,)
VINCENNES DISTRIBUTORS, INC.,)
MAX D. GELB,)
VOEGLER DISTRIBUTING CO., INC.,)
ROBERT L. HARTZ,)
WABASH COUNTY BEVERAGE CORP.,)
MRS. CHARLES DAUGHERTY,)
WABASH DISTRIBUTORS, INC.,)
DONALD G. SHAW,)
WARRICK BEVERAGE CORPORATION,)
ROBERT A. TORNATTA,)
WINCHESTER DISTRIBUTORS, INC.,)
ROBERT C. OLIVER,)
WORKING BEVERAGE, INC.,)
MILTON E. WORKING,)
YOUNG DISTRIBUTING CO., INC.,)
JAMES O. YOUNG,)
YOUNG WHOLESALE BEVERAGE, INC.,)
DARRELL YOUNG,)
)
Defendants.)

SUPPLEMENTAL COMPLAINT FOR TREBLE DAMAGES AND INJUNCTIVE RELIEF

Plaintiffs bring this action for treble damages and injunctive relief against defendants.

A.

Nature Of Claim, Jurisdiction And Venue

1. This complaint is filed and the jurisdiction of this Court is invoked pursuant to the provisions of Sections 4, 12 and 16 of the Clayton Act and 28 U.S.C. §§ 1337 and 1391(b)

and (c) to declare, to prevent and restrain, and to recover treble the amount of damages plaintiffs have suffered because of the defendants' violations of Section 1 of the Sherman Act.

2. The defendants transact business and are found within the State of Indiana and are within the jurisdiction of this Court for the purpose of service of process. Many of their unlawful acts in violation of the antitrust laws occurred within this District.

B.

Parties

3. Plaintiffs buy beer from wholesale distributors and sell it to consumers. All plaintiff business entities are organized under the laws of Indiana.

3A. The plaintiffs listed below own and operate drug stores in Indiana. They all hold beer dealers' permits issued by the State and sell carryout beer at the locations listed.

Name	Address
Arth Main Street Drugs, Inc.	1901 East Main Street Lafayette, IN
Arth Drugs, Inc.	616 West Stadium West Lafayette, IN
Arth South Fourth Drugs, Inc.	2133 South Fourth Street Lafayette, IN
Arth State Street Drugs, Inc.	306 West State Street West Lafayette, IN

3B. The plaintiffs listed below own and operate restaurants or taverns in Indiana. They all hold beer retailers' permits issued by the State and sell beer to their customers for consumption in the restaurant or tavern.

Name	Address	Name of Establishment
Otis Burkett, Inc.	721 North Main Street Rochester, IN 46975	Main Street Tavern

Name	Address	Name of Establishment
Anthony Carrara	3902 Guthrie Street East Chicago, IN 46312	Club Derby
The County Seat Hotel, Restaurant and Bar, Inc.	202 W. Washington St. Lebanon, IN 47905	The County Seat Hotel, Restaurant & Bar
CSA, Inc.	112 W. Rochester St. Akron, IN 47910	The Den
Ed's Palmer House, Inc.	18 Main Street P. O. Box 65 Chalmers, IN 47929	The Palmer House
C. R. Haddock	1319 North 14th St. Lafayette, IN	American Club Tavern
John M. Loftus	State Road 37 & U.S.30 Grovertown, IN 46531	Kate's Kozy Korner
Alex Papp	3492 Massachusetts St. Gary, IN 46409	A & M Tavern
Walkerton Star Cafe, Inc.	1004 Roosevelt Road Walkerton, IN 46574	Walkerton Star Cafe

3C. The plaintiffs listed below own and operate package stores in Indiana. They all hold beer dealers' permits issued by the State and sell carryout beer.

Name	Address	Name of Establishment
Bar Barry Liquor Store, Inc.	1110 Sagamore Pkwy. W. West Lafayette, IN	Bar Barry Liquor Store
DeLock's #1, Inc.	1413 Indianapolis Blvd. Hammond, IN	DeLock's #1
DeLock's #3, Inc.	6518 Columbia Avenue Hammond, IN	DeLock's #3
DeLock's #6, Inc.	810 Ridge Road Munster, IN 46321	DeLock's #6
DeLock's #11, Inc.	1939 169th Street Hammond, IN 46324	DeLock's #11
DeLock's #14, Inc.	5 Gostlin Street Hammond, IN 46327	DeLock's #14
Clarence W. Epley, Jr.	Culver, IN 47511	Town & Country Package Store
Mary Evans	1509 E. Michigan Blvd. Michigan City, IN 46360	East Side Liquors
Eddie C. Hardin	4101 Wheeling Muncie, IN 47304	Suburban Liquor Centre
R. L. Hatcher, Inc.	1550 169th Street Hammond, IN 46324	Cramer's Liquors

Name	Address	Name of Establishment
John W. Janes III James M. Hackleman	205 W. 29th St. Anderson, IN (4 locations)	Keg 'N Bottle
Kary-Out Corp.	287 S. Cass St. Wabash, IN 47992 (2 locations)	Kary-Out
Edmund R. Lelito	1312 Route 30 Schererville, IN 46374	Lelito's Liquors
Meyers Ventures, Inc.	6505 Calumet Ave. Hammond, IN 46324	Holiday Discount Liquors
J & M Moore, Inc.	State Rd. 43 Brookston, IN 47923	Brookston Package Store
Northcrest Liquor Store, Inc.	1110 North College Bloomington, IN 47401	Blair's Big Red Liquors
O'Hanlon, Inc.	1935 Lincolnway East South Bend, IN 46613	O'Hanlon's Warehouse Liquors
Westville Liquors, Inc.	U.S. 421 and Main St. Westville, IN 46391	Westville Package Liquor Store
21st Amendment, Inc.	5959 N. Michigan Road Indianapolis, IN 46208 (10 locations)	21st Amendment

3D. The plaintiffs listed below own and operate grocery stores in Indiana. They all hold permits issued by the State and sell carryout beer at the locations indicated.

Name	Address
J & J Thriftway Supermarkets, Inc.	360 Brown Street Levee West Lafayette, IN 47906
Nichols' Thriftway Supermarket, Inc.	1416 West State Street West Lafayette, IN 47906
Thriftway Quality Foods, Inc.	1812 Northwestern West Lafayette, IN 47906

3E. Until January, 1978, plaintiff Earl Fuller owned and operated a tavern known as Earl's Bar, 1802 Schuyler, Lafayette, Indiana 47904. He held a beer retailer's permit issued by the State and sold beer to his customers for consumption in the tavern.

3F. Until January, 1978, plaintiff Antfahl, Inc. ("Antfahl") owned and operated a tavern known as The Coach Room, 2650 Coliseum Boulevard, Fort Wayne, Indiana. Antfahl held a beer retailer's permit issued by the State, and sold beer to its customers for consumption in the tavern as well as carryout beer. Antfahl now owns and operates a tavern known as The Dugout, 3401 Fairfield Avenue, Fort Wayne, Indiana 46806. Antfahl holds a beer retailer's permit issued by the State, and sells beer to its customers for consumption in the tavern as well as carryout beer.

4A. Defendant Beer Distributors of Indiana, Inc. (the "BDI") is a not-for-profit corporation organized under the laws of Indiana with its principal place of business in Indianapolis. It is a trade association composed of Indiana beer wholesalers and other members. It has the avowed purposes of building "good will," establishing "responsibility in the industry," promoting "strict observance of the law" and advancing "moderation."

4B. The defendants listed below own and operate wholesale beer distributorships in Indiana. They all hold beer wholesalers' permits issued by the State. All defendant business entities are organized under the laws of Indiana. These defendants buy beer from brewers and sell it to retail outlets.

Name	Address
AALCO Distributing Co., Inc.	909 Grant Avenue Ft. Wayne, IN 46803
A-1 Beverage Co., Inc.	633 North Morton Street Bloomington, IN 47401
A. B. Beverage Co., Inc.	216 High Street Brookville, IN 47012
Ace Beverage Co., Inc.	631 East New York Street Indianapolis, IN 46202
Acme Beverage, Inc.	515 North 6th Street Richmond, IN 47374
Adams Distributing Co., Inc.	West Adams Street Extended P. O. Box 150 Decatur, IN 46804

Name	Address
Allen Products, Inc.	6930 Gettysburg Pike Fort Wayne, IN 46804
Angola Distributors, Inc.	313 East Mechanic Street Angola, IN 46703
B & G Distributor Co., Inc.	13 South Meridian P. O. Box 182 Brazil, IN 47834
Barco Beverage Corp.	1401 California Street Columbus, IN 47201
Bartholomew County Beverage Co., Inc.	2600 North Hawcreek Blvd. Columbus, IN 47201
Best Beers of Bloomington, Inc.	3150 South State Road #37 Bloomington, IN 47401
Better Brands, Inc.	510 Morland Drive P. O. Box 1129 Lafayette, IN 47905
Bill's Beverage, Inc.	1501 North 2nd Avenue Evansville, IN 47710
Biltz Beer Distributors	1675 North Ninth Street P. O. Box 1266 Lafayette, IN 46905
Blue River Products, Inc.	305 East Main Cross Street Edinburg, IN 46124
Boone Beverages, Inc.	1206 West South Street Lebanon, IN 46052
Brentlinger Dist. Co., Inc.	960 Spruce Street P. O. Box 1464 Terre Haute, IN 47808
Broadway Beverage	1420 Chest Street P. O. Box 558 Anderson, IN 46015
Brown Beverages, Inc.	210 East 2nd Street Seymour, IN 47905
Brown County Beverage	Hwy. 135, R. R. #2 Nashville, IN
Brumm Distributing Co., Inc.	2552 Industrial Drive Highland, IN 46322
B-F Beverage Co., Inc.	1102-08 Stadium Drive Indianapolis, IN 46202
C & J Beverage Co., Inc.	801 West 3rd Street Rushville, IN 46173
Calumet Breweries, Inc.	6535 Osburn Hammond, IN 46320

Name	Address
Cavanaugh Malt Beverage, Inc.	400 West National Highway Washington, IN 47501
Central Beverage Co., Inc.	4226 Vogel Road Evansville, IN 47715
Central Beverage Co., Inc.	616 South Elm Street Muncie, IN 47305
Central Distributing Co., Inc.	1313-15 Washington Street Gary, IN 46407
Central Distributor of Marion, Inc.	1017 South Washington Street Marion, IN 46016
City Beverage, Inc.	1103 Riverside Drive Huntington, IN 46750
City Beverage of Logansport, Inc.	635 South Burlington Avenue Logansport, IN 46947
Clark County Beverage Co., Inc.	1630 Fabricon Boulevard P. O. Box 853 Jeffersonville, IN 47130
Clark County Distributing Co., Inc.	1702 Dutch Lane Jeffersonville, IN 47130
Columbia City Beverage Co.	101 Collins Street Columbia City, IN 46725
Columbus Beverage, Inc.	1225 11th Street Columbus, IN 47201
Connersville City Beverage, Inc.	1023 Eastern Avenue Connersville, IN 47331
Couden Distributors, Inc.	639 Connor Street Noblesville, IN 46060
C'Ville Beverage Co., Inc.	912 West Main Street Crawfordsville, IN 47933
D & B Beverage, Inc.	Illinois & First Streets Petersburg Industrial Park Petersburg, IN 47567
D'Andrea Distributing Co., Inc.	421 High Street Logansport, IN 46974
Ben Daulton Distributing Co., Inc.	1703 Jefferson Rochester, IN 46975
Decatur Beverage Co., Inc.	132-4 West Railroad Street Greensburg, IN 47240
DeKalb Distributing Co., Inc.	1102 South Indiana Avenue Auburn, IN 46706

Name	Address
Delaware Beer Co.	620 South High Muncie, IN 47305
Derr's, Inc.	711 South Fifth Street P. O. Box 311 Booneville, IN 47601
Dever Distributing Co., Inc.	939 Poplar Street Terre Haute, IN 47807
Dubois County Beverage Co., Inc.	30th & Virginia P. O. Box 201 Jasper, IN
Elkhart County Beverage Co., Inc.	1700 West Lusher Avenue Elkhart, IN 46514
Elkhart Distributing Corporation	640 Riverview Avenue Elkhart, IN 46514
Dick Elliott Distributors, Inc.	1001 17th Street Logansport, IN 46947
Excel Distributing Corp.	111 West Jefferson Albion, IN 46701
Farber Distributing Co., Inc.	1421-27 North Senate Avenue Indianapolis, IN 46202
Fayette Refreshment Corp.	114 East 6th Street Connersville, IN 47331
Fedder Distributing, Inc.	201 Dyson Street Michigan City, IN 46360
Floyd County Beverage, Inc.	322 East 15th Street New Albany, IN 47150
Focht Beverage Co., Inc.	400 North 10th Street Richmond, IN 47374
Fowler Beverage Co., Inc.	401 East 8th Street Fowler, IN 47944
Friendly Beverages, Inc.	1719 English Avenue Indianapolis, IN 46201
Fulton County Beverage Distributors, Inc.	330 Main Street Rochester, IN 46975
G & K Wholesale Beverage Co., Inc.	102 West Oak Street New Albany, IN 47150
Gem City Beverage Co., Inc.	612 West Jefferson Street Frankfort, IN 46041
General Beer Distributors, Inc.	2410 South Main Street Elkhart, IN
General Beverage, Inc.	74 Wernsing Road Jasper, IN 47546

Name	Address
Gibson County Distributing Co.	229 West Pinkney Street Princeton, IN 47670
Gold-Hart Distributing, Inc.	108 4th Street Aurora, IN 47001
Goodland Distributors, Inc.	Union at Iroquois P. O. Box 287 Goodland, IN 47948
Grant Distributors, Inc.	637 Lincoln Boulevard Marion, IN 46952
Greene County Distributing Co.	Spring St. & Henderson Road P. O. Box 7 Bloomfield, IN 47424
Greenfield Beverage Co., Inc.	R. R. #3 Greenfield, IN 46140
H & K Beverage Co., Inc.	120 1/2 West 3rd Street Connersville, IN 47331
Hamilton County Malt Beverage, Inc.	484 South 11th Street Noblesville, IN 46060
Henry County Beverage Co., Inc.	125 North 26th Street New Castle, IN 47362
W. F. Holland Distributors, Inc.	1316 Barnett Vincennes, IN 47591
The Home Beverages, Inc.	113-115 SE. 4th Street Washington, IN 47501
Hoosier Beverage Co.	1205 East Market Street Crawfordsville, IN 47933
Independent Beer Distributing Co., Inc.	Route 6 P. O. Box 11 Corydon, IN 47112
J & N Beverages, Inc.	406 South 15th Street Vincennes, IN 47591
Jasper Beverage Co., Inc.	2811 Market Street Jasper, IN 47546
Jay County Beverage, Inc.	1008 North Morton Street P. O. Box 1004 Portland, IN 47371
Jefferson County Beverage Co., Inc.	1708 Cragmont Madison, IN 47250
Jennings Beverage Co., Inc.	417 Hoosier Street North Vernon, IN 47265
Johnson County Beverage, Inc.	699 Earlywood Drive Franklin, IN 47265
Juerling Beverage Corp.	North 7th & Neff Streets Richmond, IN 47374

Name	Address
J. W. Beverage Co., Inc.	1401 Walnut Avenue Frankfort, IN 46041
K & H Distributing Co., Inc.	310 North Cedar Street Warsaw, IN 46580
Kendallville Distributors Corp.	224-226 West North P. O. Box 635 Kendallville, IN 46755
Keystone Beverage Co., Inc.	1214 Green Street Richmond, IN 47374
Knox County Beverage Co., Inc.	2409 Chestnut Street P. O. Box 624 Vincennes, IN 47591
Kosciusko Beverage Co., Inc.	107 East Pearl Street P. O. Box 7 Syracuse, IN 46567
Kuhn Beer Distributors, Inc.	1815 Washington Street Michigan City, IN 46360
Lafayette Beverage Distributors, Inc.	705 South Earl Avenue Lafayette, IN 47902
Lakes Beverage Co., Inc. of Monticello	522 North Dewey Street P. O. Box 613 Monticello, IN 47902
Lake County Beverage Corp.	3790 Grant Street Gary, IN 46408
LaPorte County Beverage Co., Inc.	700 West 6th Street Michigan City, IN 46360
Lawrence County Beverage Co., Inc.	727 14th Street Bedford, IN 47421
Leslie-Powers Distributors, Inc.	West Division Street P. O. Box 261 Booneville, IN 47601
Lester Beverages, Inc.	927 Shields Avenue Seymour, IN 47274
Lincoln Hills Beverage Co., Inc.	1348 12th Street Tell City, IN 47586
Linton Beer Sales, Inc.	317 South Main Street Linton, IN 47441
Liquids, Inc.	1 Main Street Anderson, IN 46016
Little Beverage Company	103 West Sycamore Street Attica, IN 47918
Local Beers, Inc.	1324 Tell Street Tell City, IN 47586

Name	Address
Loogootee-Shoals Beverage Co., Inc.	205-207 East Main Street P. O. Box 135 Loogootee, IN 47553
Lowry Wholesale Beverage, Inc.	1301 North 9th Street P. O. Box 383 Clinton, IN 47842
Ed J. Luther Beverages, Inc.	112 North Niles Avenue South Bend, IN 46617
Mace & Sons, Inc.	234 Kinney Street Muncie, IN 47302
Maco Beverage Corporation	1803 Columbus Avenue Anderson, IN 46016
Madison Distributing Co.	100 West 5th Madison, IN 47250
Magic City Beverage Company, Inc.	2700 South Monroe Street Muncie, IN 47302
Marion Distributing Co., Inc.	413 West 9th Street Marion, IN 46952
Marshall County Beverage Co., Inc.	702 West Jefferson Street Plymouth, IN 46563
Martin County Distributors, Inc.	106 Mill Street Loogootee, IN 47553
Michiana Beverages, Inc.	142 South Olive Street South Bend, IN 46628
Miller Beverage, Inc.	1020 North Main Street Kokomo, IN 46901
Monarch Beverage Co., Inc.	116 East Market Street P. O. Box 438 Indianapolis, IN 46206
Montgomery County Beverage Co., Inc.	605 Lafayette Ave. P. O. Box 109 Crawfordsville, IN 47933
Monroe Beverage Co., Inc.	220 West Allen Bloomington, IN 47401
Morgan County Beverage, Inc.	189 West Walnut Street Martinsville, IN 46151
Morrison Beverage, Inc.	210 West Franklin P. O. Box 88 Delphi, IN 46923
Leo J. Murphy, Inc.	501 West Knight Street Brazil, IN 47834
Nachand Beverage Company, Inc.	315 East 10th Street Jeffersonville, IN 47130

Name	Address
L. C. Nadorff & Son, Inc.	1818-20 East Market Street New Albany, IN 47150
Noble County Beverage Co., Inc.	100 South Calvin Street Ligonier, IN 46767
Norris Beverage, Inc.	208 South 16th Street New Castle, IN 47362
North Vernon Beverage Co., Inc.	502 North 5th Street North Vernon, IN 47265
Ohio Valley Beverage Co., Inc.	Box 330, U.S. 50 West Aurora, IN 47001
Old Capitol Beverage Co., Inc.	R. R. 5, Box 169A Corydon, IN 47112
Orange County Beverage Co., Inc.	112-114 Wells Avenue P. O. Box 32 French Lick, IN 47432
Patoka Valley Beverage Corp.	402 McCrillus Street P. O. Box 607 Jasper, IN 47546
Pfeifer Distributing Co., Inc.	1024 Crawford Street Terre Haute, IN 47807
Pocket Beverage Company, Inc.	2103 North Kentucky Avenue Evansville, IN 47717
Pollard & Burton, Inc.	1401 East Broadway P. O. Box 449 Princeton, IN 47670
Polster Beverage Corporation	Old Lincoln Trail Evanston, IN 47531
Posey County Beverage Co., Inc.	1000 North Main Street Mt. Vernon, IN 47620
Putnam Beverages, Inc.	500 North Jackson Greencastle, IN 46135
Quality Beers, Inc.	1400 Canal Road Lafayette, IN 47902
Red Bright Beer Distributing Co., Inc.	1200 6th Avenue Terre Haute, IN 47807
Rhoads Beverage Co., Inc.	706 West Main Street Plainfield, IN 46168
The Ripley County Beverage Co., Inc.	912 East Pearl Street Batesville, IN 47006
Ripley County Wholesalers, Inc.	North Main Street P. O. Box 36 Milan, IN 47031

Name	Address
Rockville Wholesale Corporation	115 East Pennsylvania P. O. Box 97 Rockville, IN 47872
Rush County Beverage Co., Inc.	126 South Perkins Street P. O. Box 135 Vevay, IN 47043
S & O Beverage Corp.	610 Ferry Street P. O. Box 135 Vevay, IN 47043
Salem Beverage Co., Inc.	307 South Water Street Salem, IN
Schembre Beverage Co., Inc.	1432 South Union Street Kokomo, IN 46901
Scott County Beverage Co., Inc.	R. R. 6, Box 336 Scottsburg, IN 47170
Scott County Distributing	505 East McClain Avenue Scottsburg, IN 47170
The Shannon Corporation	414 East South Street Shelbyville, IN 46176
Shelco Beverage, Inc.	62 3rd Street Shelbyville, IN 46176
Southeastern Beverages, Inc.	439 George Street Lawrenceburg, IN 47025
Spencer County Beverage Co., Inc.	H. 45 & North Street P. O. Box 67 Chrisney, IN 47611
Springer, Inc. d/b/a Wabash Beverage	812 South Main Street Sullivan, IN 47822
Starke County Beverage Co., Inc.	51-53 West Mound Street Knox, IN 46534
Sullivan County Distributing, Inc.	219 West Illinois Street Sullivan, IN 47882
Sunnyside Beverages, Inc.	1340 South Bend Avenue South Bend, IN 46617
Tell City Beverage Co., Inc.	1047 12th Street Tell City, IN 47586
Three Rivers Beverage Co.	1515 Dividend Road Fort Wayne, IN 46808
Todd & Justak, Inc.	3721 East 10th Street Indianapolis, IN 46201
Town & Country Beverages, Inc.	732 East Fordice Street Lebanon, IN 46052

Name	Address
Tree City Beverage, Inc.	1032 North Anderson Street Greensburg, IN 47240
Tri-City Beverage Co., Inc.	4526 Baring Avenue East Chicago, IN 46312
Tri-State Beverage Co.	320 Monroe Avenue - Rear Evansville, IN 47712
United Beverage Co. of South Bend, Inc.	840 Prairie Avenue South Bend, IN 46621
Valley Beverage Co.	805 South Cleveland Street Mishawaka, IN 46544
Valpo Beverages, Inc.	825 Elm Street P. O. Box 123 Valparaiso, IN 46303
Vanco Beverage, Inc.	2400 North Fulton Avenue Evansville, IN 47710
Vermillion Beverage, Inc.	105 Blackman Street P. O. Box 384 Clinton, IN 47842
Vincennes Distributors, Inc.	2810 Old Decker Road Vincennes, IN 47591
Voegler Distributing Co., Inc.	102 "L" Street P. O. Box 427 LaPorte, IN 46350
Wabash County Beverage Corp.	250 Olive Street P. O. Box 213 Wabash, IN 46992
Wabash Distributors, Inc.	45 East Harrison Avenue Wabash, IN 46992
Warrick Beverage Corporation	115 West Jefferson Avenue P. O. Box 369 Chandler, IN 47610
Winchester Distributors, Inc.	230 West Franklin Street P. O. Box 148 Winchester, IN 47394
Working Beverage, Inc.	703 Oak Hill Road Evansville, IN 47711
Young Distributing Co., Inc.	919 Millbrook Lane Kokomo, IN 46901
Young Wholesale Beverage, Inc.	307 South Main Street Salem, IN 47167

4C. The individual defendants are associated with the various wholesale distributors named as defendants. They are residents of Indiana and most, if not all, are active in the BDI.

Name	Address
Richard D. Jones	909 Grant Avenue Ft. Wayne, IN 46803
Clyde Fiscus	633 North Morton Street Bloomington, IN 47401
Marie P. Brown	216 High Street Brookville, IN 47012
Edwin Ratcliffe	631 East New York Street Indianapolis, IN 46202
Richard K. Brinker	515 North 6th Street Richmond, IN 47374
W. A. Klepper	West Adams Street Extended P. O. Box 150 Decatur, IN 46804
Sid Hutner	6930 Gettysburg Pike Fort Wayne, IN 46804
Edward J. Williams	313 East Mechanic Street Angola, IN 46703
Paul O. Gorham	13 South Meridian P. O. Box 182 Brazil, IN 47834
Robert V. Welmer	1401 California Street Columbus, IN 47201
Francis M. Overstreet	2600 North Hawcreek Blvd. Columbus, IN 47201
Robert A. Haak	3150 South State Road #37 Bloomington, IN 47401
Tom Brodsky	510 Morland Drive P. O. Box 1129 Lafayette, IN 47905
Louanna Young	1501 North 2nd Avenue Evansville, IN 47710
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Wayne Kellams	305 East Main Cross Street Edinburg, IN 46124
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Name	Address
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Bernard J. Montgomery	801 West 3rd Street Rushville, IN 46173
George E. Kiernan	6535 Osburn Hammond, IN 46320
Mrs. George Cavanaugh	400 West National Highway Washington, IN 47501
W. R. Scott	4226 Vogel Road Evansville, IN 47715
Eugene C. Turner	616 South Elm Street Muncie, IN 47305
Joseph Buley	1313-15 Washington Street Gary, IN 46407
Sam J. Coniglio	1017 South Washington Street Marion, IN 46016
Michael T. Fisher	1103 Riverside Drive Huntington, IN 46750
John T. Cotner	635 South Burlington Avenue Logansport, IN 46947
Floyd Throckmorton	1630 Fabricon Boulevard P. O. Box 853 Jeffersonville, IN 47130
Ira B. McKinley	1702 Dutch Lane Jeffersonville, IN 47130
Henry A. Sievers	101 Collins Street Columbia City, IN 46725
Helen I. Sievers	101 Collins Street Columbia City, IN 46725
Erma R. Collier	1225 11th Street Columbus, IN 47201
Cloyce Blue	1023 Eastern Avenue Connersville, IN 47331
Joseph R. Couden	639 Connor Street Noblesville, IN 46060
James Stephens	912 West Main Street Crawfordsville, IN 47933

Name	Address
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Resto D'Andrea	421 High Street Logansport, IN 46974
Ben Daulton	1703 Jefferson Rochester, IN 46975
William E. Crister	132-4 West Railroad Street Greensburg, IN 47240
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Helen McKenna	114 East 6th Street Connersville, IN 47331
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B. B. Overholser	401 East 8th Street Fowler, IN 47944

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John L. Kirkpatrick	R. R. #3 Greenfield, IN 46140
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George Leininger	1708 Cragmont Madison, IN 47250
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Roy V. Calkin, Jr.	1214 Green Street Richmond, IN 47374
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Karl J. Kuhn	1815 Washington Street Michigan City, IN 46360
James E. Lamb	705 South Earl Avenue Lafayette, IN 47902
Jack Macy	522 North Dewey Street P. O. Box 613 Monticello, IN 47902
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Francis D. Baker	317 South Main Street Linton, IN 47441
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James B. Wallace	103 West Sycamore Street Attica, IN 47918
James H. Bruggenschmidt	1325 Tell Street Tell City, IN 47586
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Kenneth L. Shively	2700 South Monroe Street Muncie, IN 47302
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Richard Morrison	210 West Franklin P. O. Box 88 Delphi, IN 46923
Jerry Johnson	501 West Knight Street Brazil, IN 47834
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Darrell Young	307 South Main Street Salem, IN 47167

C.

Co-Conspirators

5. Other corporations, individuals and other entities which are not named as defendants in this complaint participated as co-conspirators in the offenses charged herein and performed acts and made statements to further the conspiracy.

D.

Economic and Historical Background

6. The wholesale distribution of beer is a significant industry in Indiana. Shipments from breweries to wholesalers in the State during 1976 totalled 98,176,933 gallons, a 4.9% increase over 1975 shipments. In the first quarter of 1977, shipments have increased 3.9% over the comparable 1976 period of 31,088,559 gallons.

7. In Indiana, as in most states, beer sales are dominated by large breweries that distribute their brands throughout the United States on a national or regional basis. In 1976, the top ten sellers in Indidna -- Pabst, Stroh, Anheuser-Busch, Heileman, Miller, Schlitz, Falstaff, Falls City, Olympia and Carling-National -- accounted for 96.6% of total shipments. The top five produced 81.7% of total shipments.

8. Although at one time there were many breweries located in Indiana, the number has steadily decreased so that today only the old Sterling brewery in Evansville and a Falstaff plant in Ft. Wayne remain and both of those are now owned by foreign corporations. Thus, shipments of beer into Indiana from other states far surpass in-state production. In the first quarter of 1977, the out-of-state brewers produced 94.5% of the beer sold within Indiana and the amount of beer physically brewed outside the State is an even larger percentage. This beer produced outside Indiana is generally brought into the State via the trucks of the wholesale distributors. The retailers who purchase from the distributors in turn resell substantial quantities of beer to citizens of foreign states. The wholesale distribution and sale of beer thus constitutes and substantially affects trade and commerce among the several states within the meaning of Section 1 of the Sherman Act.

9. Since the repeal of Prohibition, the wholesale distribution of beer in Indiana has been what the BDI once described as "orderly." "Orderly" was really an euphemistic description of exclusive territorial allocation or confinement. There was a "system," eventually called the "BDI System" that, simply translated, prohibited more than one

wholesale distributor for a given brand of beer from selling in a given market. With the exception of the more rural areas of the State, the given territory was generally a particular county. Thus, if a wholesale distributor was located, for instance, in Tippecanoe County, he could not sell to retailers in Carroll or White County. He was limited to one county. The BDI System was created and enforced by a "gentleman's agreement" among wholesale distributors and others throughout Indiana, including the defendants. The BDI System was neither mandated nor authorized by Indiana law or any rule or regulation of the Indiana Alcoholic Beverage Commission. This lack of legal authorization for the BDI System at all times was known by the defendants and led to their unsuccessful efforts in the past several sessions of the Indiana General Assembly to secure enactment of the so-called "Beer Baron Bill," which prospectively would have authorized and sanctified the BDI System.

10. Attempts to buck the BDI System have met instant retaliation. That retaliation by the defendants has not only been private and unofficial; it also has featured the use -- or more accurately the misuse -- of the courts and other governmental agencies.

11. When several wholesalers in northern Indiana began selling beer to any retail permittee that wished to purchase it, even though the purchaser resided in a county allocated by the BDI System to another wholesale distributor, defendants attempted to staunch this breach of the BDI System in several ways. First, the BDI used defendant B-F Beverage Company, Inc. to file a lawsuit against one of these wholesalers and an Indianapolis retail outlet seeking an injunction and declaration that such transactions were illegal. The BDI described this action as the ". . . first lawsuit in B.D.I's

effort to enforce the present law. . . ." The court dismissed the case because it failed to state a claim upon which relief could be granted and because the court did not have subject matter jurisdiction.

12. Then, on April 5, 1976, the BDI distributed an injunction kit to all of its wholesaler members. The BDI assumed that the wholesalers operating within the BDI System had some proprietary right to all retailers within their allocated territories by addressing the cover letter to wholesalers ". . . that have retail permittees transporting malt beverages. . . ." The BDI encouraged them ". . . to file 'verified complaints for violation of alcoholic beverage law' against the transporting retailers and the wholesalers selling to them." A form complaint with appropriate blanks was enclosed together with a "memorandum of law" for the "convenience of your local attorney."

13. Ten days later, three Vincennes wholesale distributors, defendants W. F. Holland Distributors, Inc. J & M Beverages, Inc. and Vincennes Distributors, Inc. filed another lawsuit against four Vincennes package stores and two of the northern Indiana distributors who had sold them beer seeking an injunction and declaration that would halt such sales. Again the court dismissed the case for lack of subject matter jurisdiction, and because it failed to state a claim upon which relief could be granted.

14. Defendants then attempted to cast their objections to such sales as a union/non-union dispute and promoted a boycott of certain retail package stores in Marion County by union members. However, the boycott floundered when a union official publically charged that he had been given incorrect and misleading information by the BDI.

15. Finally, 27 wholesale distributors, including companies of past and current officers and directors of the BDI, filed a suit in this court in which the putative defendants are officials of the State of Indiana. This suit also seeks to halt the extra-territorial sales.

E.

Offenses And Injuries Charged

16. Thus, beginning on a date unknown to plaintiffs and continuing to the present time, the defendants and their co-conspirators have engaged in a continuing combination and conspiracy to unreasonably restrain the trade and commerce in the wholesale distribution of beer in violation of Section 1 of the Sherman Act. Their purpose and intent was to fix, stabilize and maintain the price of beer at the highest possible level and to restrain and eliminate actual or potential competition in the wholesale distribution of beer.

17. To further and effectuate this conspiracy they:

(a) allocated among themselves the geographical territories in which each would sell beer;

(b) restricted the geographical territories within which retailers could purchase beer;

(c) established, stabilized and maintained uniform prices for beer; and

(d) engaged in and encouraged sham litigation and other similar resorts to governmental agencies.

18. As a result of their acts, the price of beer has been higher than it otherwise would have been, and plaintiffs have thus been injured in their businesses and other property.

The amount of damages thus sustained by plaintiffs cannot be precisely ascertained until discovery is concluded.

19. Plaintiffs are threatened with further loss and damage unless the defendants' antitrust violations are enjoined.

F.

Fraudulent Concealment

20. Plaintiffs had no knowledge of the antitrust violations alleged herein, nor of any facts which might reasonably have led to the discovery thereof until sometime in October of 1975 at the earliest. Plaintiffs could not have discovered these violations at an earlier date by the exercise of due diligence because of the deceptive practices and techniques of secrecy employed by the defendants to avoid detection and to fraudulently conceal the true nature of their conduct.

G.

Relief Requested

WHEREFORE, plaintiffs request that the Court:

1. Adjudge that, as alleged above, the defendants have violated Section 1 of the Sherman Act;

2. Permanently enjoin the defendants from directly or indirectly continuing or reviving these violations;

3. Enter judgment entitling plaintiffs to recover from the defendants threefold the damages sustained and the costs of this action, including a reasonable attorneys' fee; and

4. Grant such other further relief as may be necessary and appropriate.

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The CHAIRMAN. You may care to answer the previous witness, if you would like to, Ms. Eleanor Fox, professor of law at New York University. You heard her testimony, didn't you? If either one of you would care to comment on that, you may do so.

Mr. RIDDELL. Mr. Chairman, I represent the U.S. Brewers' Association. My name is James Riddell. I am a partner in the firm of Dawson and Riddell. We have submitted statements for the record.

I am here to describe the industry, the problem, and to answer questions. I am pleased to have an opportunity to answer Ms. Fox and the Federal Trade Commission witness.

First——

The CHAIRMAN. You heard Mr. Winslow's testimony, didn't you?

Mr. RIDDELL. Yes, I did.

The CHAIRMAN. And you heard Ms. Fox's?

Mr. RIDDELL. Yes, I did.

The CHAIRMAN. Now, you may say anything you wish, and then respond to them, if you care to.

Mr. RIDDELL. Well, let us begin by pointing out that Ms. Fox is relying upon a study supposedly conducted in the State of Indiana, which purports to show that their prices in Indiana have dropped 20 percent. There is no such study, and none has been produced for this committee's inspection, and insofar as I know, there is not a scintilla of evidence to support her statement. The statements of Ms. Fox and Mr. Winslow were no more than a lot of "mights," "maybes," and unsupported fears for the future. Those fears have not been justified with respect to the soft drink industry, nor can it reasonably be said that they would be justified with respect to the brewing industry.

The brewing industry is the total creature of State law. The States have plenary power under the 21st amendment to deny us the right to even manufacture our product or to sell it. They tell us to whom we can sell it. In many instances, they tell us at what prices we must sell it.

Unlike soft drinks and other products in commerce, our distributors may not even select the customers to whom they sell. A wholesaler has a limited number of customers to whom he may sell. A retailer, in order to sell beer, must be licensed. The number of licenses is always limited. The beer wholesaler must price out his product, covering the FOB price of the beer and average excise taxes—State and Federal—of $15 a barrel. He then takes his product into the market with an overhead that he must be able to meet in order to stay in the business. If he is fortunate within his territory, he has volume customers. The volume customers are usually large chain food stores or drugstores or large chain packaging stores.

I am about to relate to you a story of greed and seduction. The large customer is dealing with the franchised or the licensed wholesaler in his district. That wholesaler has priced out. He has already given him a discount in price, if it is legal under the State to do so. He is buying 50,000 cases. He says, "You are charging me $2 a case."

He goes to another wholesaler outside of the State, or within the State, and says, "I am buying 50,000 cases. If you will give me a price of $1.75, I will give you all of my business."

He makes that arrangement, and free riding begins. The next chain of grocery stores says, "If he can get away with it, I will do it," so he seduces another wholesaler, and so on. Finally, my wholesaler, as you have heard here, is reduced to nothing. He has no one in his territory to whom he can sell and justify his continued business. And yet, he is bound to drive his truck the same 8 miles, to put out 15 cases that he used to drive to put out 2,000. And the legitimate wholesaler is being destroyed by, as I say, greed and seduction.

The Federal Trade Commission's point is not well taken. There is no evidence that the soft drink bill has led to any of the "mights" or "maybes" that he indicated. Furthermore, the industry is so subject to regulation that we may be put out of business at any time, by any State authority who chooses to do so. We are the tax collector for the Federal Government, and the tax collector for the local community. We are also the enforcer of State law. If, for example, the State pulls a license on one of their grocery stores, he is responsible for seeing that the product does not get to it, and the State comes right in and says, "Why is he getting the product? I told you not to sell to him."

He says, "I am sorry about your excise taxes, and I am sorry about the beer that has shown up in that unlicensed, retail outlet. However, it was not mine."

He is also charged with picking up the bad beer that the distributor who transshipped left in the territory.

We are so regulated, Mr. Chairman, that we cannot even blink our eyes. We are the subject of constant public scrutiny. And as for the consumer, the figures of the Federal Government indicate that compared to virtually every other beverage, the consumer is well served. Using the Consumer Price Index formulated by the Department of Labor, beer is at an index today of 201; soft drinks, 296; coffee, 353; nonalcoholic beverages, including milk, 412. I mean, the consumer is well served.

Now, bear in mind, sir, that when I quote you these prices, that every container of beer bore a State tax, a Federal tax, and in many instances, a local tax, which is to say that these prices were achieved for the benefit of the consumer, even though our product carries with it an average burden of taxation of $15 a barrel.

I am distressed that Government witnesses can sit before you and say that they have seen no evidence. He has not looked. His "mights," his "maybes," his argument that the rule of reason provides shelter against a transshipper, against one of these food chains, is meaningless. We have no remedy, because the wholesaler has no money with which to pursue it.

You heard the story of harassment. The case out in Indiana that has had every wholesaler out there tied up for how many years?

Mr. **Dee**. Five years.

Mr. **Riddell**. For 5 years. The burden, sir, asked in the complaint, is $175 million, multiplied by three, and then, make me guess—I have been at the bar for 30 years—what the Federal Trade Commission would do, or what some Federal court will do. What is the point of having the law, if we cannot seek protection under it?

Let me make one more point. If the Sherman Act were repealed tomorrow, if it had never come into existence, my industry would still be in the position where it is totally controlled, is controlled, and always will be controlled. For example, there are four States in the Union, Mr. Chairman, where it is not legal for my wholesalers to sell beer to grocery stores.

The Sherman Act exists, but I do not understand how the mighty Sherman Act is sufficient to turn aside those State statutes. We would like to be able to sell in those four States to grocery stores. We would like to see our product treated like cornflakes, candy and popcorn. It is not. We bear a heavy enough burden as it is.

The only thing that this bill does is give us the right to go to the legislature and say, "Give us the right to protect ourselves in your State," and that is all.

I thank you for your indulgence, sir.

The **Chairman**. Thank you.

Is Senator MacManus here?

Mr. **MacManus**. Yes, Senator.

The **Chairman**. Senator MacManus, there is a vote on right now. I waited until the last 5 minutes, and I am going to have to rush over and vote. You are the last witness here, and I have another meeting at 11. Senator Specter of Pennsylvania will come back and finish this hearing after we vote. We have got to go and vote right now.

We thank all of you for your appearance here, and your testimony will be called to the attention of the committee members.

We will take a recess now in order to go and vote.

[Short recess.]

[Whereupon, Senator Specter assumed the Chair.]

Senator SPECTER. Senator Simpson?

Senator SIMPSON. I came to make an abject apology. I had intended to chair this entire hearing this morning, and I am most appreciative of Senator Thurmond, who then went on and did that for me, and now, I appreciate very much Senator Specter of Pennsylvania to come and conclude the hearing. As I say, I feel quite remiss and will flog myself lightly before you, and say that I have a confirmation hearing right now that I must chair on the Deputy Adiministrator of the Veterans' Administration. Senator Specter is a member of that committee. I had a debate on the floor with regard to the Mitchell amendment. And, if I were cloned, I could make it around here, but I cannot, and I just want you to know that I appreciate the distance many of you came and regret that I could not participate as fully, and I hope that both sides will feel that they have had a complete hearing on this issue at the conclusion of this hearing, that will be the second hearing that we have held.

I thank you very much, and thank you, Arlen, very much.

Senator SPECTER. Senator Simpson is one of the fastest moving men or women in the U.S. Senate. When he came to this job, how much was it you weighed, Alan?

Senator SIMPSON. 260 pounds. [Laughter.]

Senator SPECTER. He has the unique ability to be ubiquitous and effective at it. He can be in several places at one time.

We now call upon Senator Don MacManus, executive director of Rocky Mountain Food Dealers' Association, of Denver, Colo.

Welcome, Senator MacManus. We look forward to your testimony.

STATEMENT OF SENATOR DON MacMANUS, EXECUTIVE DIRECTOR, ROCKY MOUNTAIN FOOD DEALERS' ASSOCIATION, DENVER, COLO.

Mr. MACMANUS. Senator Specter, thank you very much for this opportunity.

My name is Don MacManus. I am executive director of the Rocky Mountain Food Dealers' Association, which is a trade association of retail grocers in the States of Colorado and Wyoming. Our membership is made up of 650 chain and independent food markets, convenience stores, and suppliers. Mr. Chairman, I am also serving in my fourth term, 14 year, as a member of the Colorado State Senate.

The final hat I would like to mention is the hat of first vice president of the Food Industry Association Executives, an industry professional organization with nationwide membership. The Food Industry Association Executives operates associations which have a membership of somewhere in the neighborhood of 120,000 retail food stores.

The Rocky Mountain Food Dealers Association, in its June board meeting, passed a resolution in opposition to S. 1215. The Food Industry Association executives passed a similar resolution at a general membership meeting last week in Anaheim, Calif., opposing S. 1215.

S. 1215, the Malt Beverage Interbrand Competition Act, is a grossly misnamed piece of legislation because the act would wind up preventing competition among distributors of beer. I need not tell you that competition is what keeps prices and services right. In Colorado, the brewers and distributors have their own exclusive territorial agreements to prevent different distributors of a particular brand from competing with each other.

Retailers are not thrilled with this situation, but at least there is no State statute to prevent intrabrand competition. Market conditions and philosophies could change, and competing firms could operate legally in our State. This potential for competition serves in a limited way to keep beer wholesalers honest.

I was involved in the free enterprise marketing of wholesaling to retail stores for most of my adult life. I can assure you that there is plenty of interbrand and intrabrand competition in every section of the supermarket. You can buy your different brands of juice, frozen vegetables, or whatever from a number of distributors. This is as it should be. The competitive marketing situation in the distribution of food has served us all very well. Competition, whether at the wholesale level or the retail level, means lower consumer prices.

I am sure you will agree with me that competition should be encouraged to the maximum extent possible. Yet, with this bill, beer wholesalers and brewers are asking Congress to endorse limited competition in the beer industry. Food retailers in Colorado and Wyoming and around the country simply do not understand how this can be justified in the public interest.

The most damaging thing about the monopoly distribution system advocated in S. 1215 is the lack of incentives to do a better job. Since the retailer has no choice but to carry the brand his customers demand, he is at the mercy of the designated monopolist. No matter how poor the service or how high the price, the retailer and his customers are stuck with the one supplier of product. I cannot overemphasize the difficulties encountered by retailers in this situation. Wholesalers who have monopolies are just not as responsive as they would be if they were competing for the retailer's business.

We have seen the results of monopolies in other industries that are protected from competition by regulation. For example, in the transit systems that I am familiar with, rude, uncooperative service and poor scheduling seems to be the rule, not the exception.

When I was a freshman legislator in the Colorado Assembly, a wise old senator told me to beware of businessmen who were pleading to be regulated or protected. Far too often, these interests are seeking regulation to keep competition out.

I will never forget the verbal abuse that I received from a constituent who had bought a truck and advertised himself as being in the moving and storage business, and then found himself charged with a criminal offense. It turned out that the entrance barriers in the trucking business kept new competition out, resulting in higher prices to consumers and higher profits for truckers already in business. These barriers are now falling across the country at the Federal level, of course, and at the State level. It certainly would be incongruous for the Federal Government to endorse new entrance barriers in the beer distributing business now. There is simply no danger to the public interest that requires the beer industry to be protected from competition.

I have asked my friends who are in the beer distribution business in Colorado why it is they need the protection afforded them in S. 1215. They say that malt beverage products have a short life and they need to see that retailers do not overbuy, store improperly, and that they rotate the product.

First, the shelf life of beer is 75 to 120 days, far more than the produce we handle so successfully every day.

Second, retailers are smart buyers of over 9,000 items on their shelves; if they are not good, they are out of business real quick. Supermarket personnel handle and rotate far more perishable items than beer—to name a few: frozen foods, flowers, produce, dairy products, fresh meats, and a host of others. Our industry is good with products which require questionable treatment.

Senator SPECTER. Excuse me, Senator MacManus. You have just a minute left. We have your full statement, and it will be made a part of the record. And within the time remaining, if you would summarize, we would appreciate it.

Mr. MACMANUS. I want to point out to you, Senator, that the 21st amendment does give to the States the right to regulate the distribution of alcoholic beverages and that this bill intrudes on that right. You have heard from individuals in the beer distribution business, who are fearful that competition will put them out of business. These people distributing beer have not lived in the same world with the bulk of those who distribute other food products, or any other product, for that matter. The fear of going out of business is in the back of the mind of all of us who are in business.

However, Government protection is certainly not the answer. S. 1215 is a protection from competition that is unwarranted, and certainly unnecessary.

I would be glad to answer any questions.

[The following was received for the record.]

STATEMENT

OF

DON MACMANUS

ROCKY MOUNTAIN FOOD DEALERS ASSOCIATION

Thank you for this opportunity, Mr. Chairman. My name is Don MacManus; I am the Executive Director of the Rocky Mountain Food Dealers Association, the trade association of the retail grocers of the states of Colorado and Wyoming. Our membership is made up of over 650 chain and independent food markets, convenience stores and suppliers.

Mr. Chairman, I am also serving in my fourth term as a member of the Colorado State Senate.

The final hat I would like to mention is the hat of first Vice President of the Food Industry Association Executives, an industry professional organization with nationwide membership. The Food Industry Association Executives represent somewhere in the neighborhood of 120,000 retail food stores.

The Rocky Mountain Food Dealers Association, in it's June board meeting, passed a resolution in opposition to S. 1215. The Food Industry Executives passed a similar resolution at a general membership meeting last week in Anaheim, California, opposing S. 1215.

S. 1215, the Malt Beverage Interbrand Competition Act, is a grossly misnamed piece of legislation because the act would wind up preventing competition among distributors of beer. I do not need to tell you that competition is what keeps prices and service right. In Colorado the brewers and distributors have their own exclusive territorial agreements to prevent different distributors of a particular brand from competing with each other. Retailers are not thrilled with this situation, but at least there is no state statute to prevent intrabrand competition. Market conditions and philosophies could change and competing firms could operate legally in our state. This potential for competition serves in a limited way to keep beer wholesalers honest.

Senator Simpson, as you know, the law, for practical purposes, in Wyoming prevents beer sales in food stores. Anti-competitive liquor interests are so strong in the Wyoming General Assembly that the retail food industry is very strongly considering going to the people via a referendum to obtain beer sale priviliges. Be assured, we will be careful with the wording in the proposed referendum so that exclusive territories will not be sanctioned.

I was involved in the free competitive market of wholesaling to retail food stores for most of my adult life. I can assure you that there is plenty of interbrand and intrabrand competition in every section of the supermarket. You can buy your different brands of juice, frozen vegetables or whatever from any number of distributors. This is as it should be. The competitive marketing situation in the distribution of food has served us well. Competition whether at the wholesale or retail level means lower consumer prices.

I am sure you agree with me that competition should be encouraged to the maximum extent possible. Yet with this bill, beer wholesalers and brewers are asking Congress to endorse limited competition in the beer industry. Food retailers in Colorado and Wyoming and around the Country simply do not understand how this can be justified as in the public interest.

The most damaging thing about the monopoly distribution system advocated in S. 1215 is the lack of incentives to do a better job. Since the retailer has no choice but to carry the brands his customers demand, he is at the mercy of the designated monopolist. No matter how poor the service or how high the price the retailer and his customers are stuck with the one supplier of product. I can't overemphasize the difficulties encountered by retailers in this situation. Wholesalers who have monopolies are just not as responsive as they would be if they were competing for the retailer's business.

We have seen the results of monopolies in industries that are protected from competition by regulation. Think about our exclusive urban transit systems. Rude, uncooperative service and poor scheduling seems to be the rule, not the exception.

When I was a freshman legislator, a wise old senator told me to beware of businessmen who come pleading to be regulated or protected. Far too often, these interests are seeking regulation to keep competition out.

I will never forget the verbal abuse I received from a constituent who bought a truck and advertised himself as being in the moving and storage business, and found himself charged with a criminal offense. It turned out that the entrance barriers in the trucking business kept new competition out resulting in higher prices to consumers and higher profits for truckers already in business. These barriers are now falling across the country both at the federal and state level. It certainly would be incongruous for the federal government to endorse new entrance barriers in the beer distributing business now. There is simply no danger to the public interest that requires the beer industry to be protected from competition.

I have asked my friends who are in the beer distribution business in Colorado why they need the protection afforded them in S. 1215. They say that malt beverage products have a short shelf life and they need to see that retailers don't overbuy, store improperly, and that they rotate the product.

First, the shelf life of beer is 75 to 120 days, far more than the produce we handle quite successfully.

Second, retailers are smart buyers of some 9,000 items on their shelves; if they aren't good, they're out of business, quick. Supermarket personnel handle and rotate far more perishable items than beer (to name a few: frozen foods, flowers, produce, dairy products, fresh meats and a host of others). Our industry is good with products which require special treatment. Exclusive territories are certainly not needed to guarantee fresh products.

Beer distributors point to territorial sanctions created for soft drink bottlers, but the monopoly territories created under S. 1215 is special treatment for beer wholesalers who are entirely different than soft drink bottlers. Soft drink bottler's have a significant capital outlay for bottling equipment which puts them into an entirely different scenario.

Not only does S. 1215 intrude into the competitive marketplace unnecessarily, but I would say it is an intrusion into the states' rights to regulate the distribution of alcoholic beverages within their borders under the 21st amendment. In fact, I would state that the argument offered by proponents that this bill simply clarifies the states' rights under the 21st amendment, is probably one of the grossest distortions I have heard in all my years in politics.

First of all, there is no uncertainty about the states' rights under the 21st amendment or about the fact that the antitrust laws do apply to the alcoholic beverage industry despite the existence of the 21st amendment. But more importantly, even if there were confusion in this area, this bill does not provide an exemption for state activity. Rather, it goes far beyond that and provides special treatment under the antitrust laws for the arrangements between brewers and beer wholesalers, without any requirement of state activity. If a state has no law one way or the other on the necessity for exclusive territories for beer wholesalers, the language of S. 1215 would still apply and would immunize such private arrangements under the antitrust laws.

Mr. Chairman, if the state legislatures in Wyoming and/or Colorado were to choose to require exclusive territories for beer distributors and were, through their alcoholic beverage control boards, to actively supervise the distribution system, then I might disagree with that result. I would not, however, quarrel with the states' rights to do that. But as I have stated, S. 1215 has nothing to do with that right. Providing an exemption from the antitrust laws for such arrangements without any state action simply allows brewers and wholesalers to enter into these arrangements in those states with impunity. That is exactly why they want this legislation.

We in the states are in a deregulating mood and we do not appreciate industries, like the beer industry, coming to Washington for protection they have been unable to obtain from the state legislatures. As someone who is proud to have sponsored, nurtured and helped with the passage of the nation's first "sunset" act, I urge you not to protect a brand new industry from competition.

Of course, by now you have heard the strong opposing testimony of the Food Marketing Institute, from directors of retail councils, supermarket operators, state and regional food trade associations, restaurant and bar owners, the Federal Trade Commission, the Department of Justice and others. Mr. Chairman, and members of the Committee, the tide has turned against special treatment legislation. This type of legislation, in the long run, costs the poor, old, long-suffering consumer right in his poor, old, long-suffering pocket.

I urge you to deep six this anti-consumer, anti-free enterprise legislation as soon as possible. Thank you.

Senator SPECTER. Thank you very much, Senator.

I regret that Senator Thurmond and Senator Simpson could not be here, but your testimony will be made available to the entire committee.

Mr. MACMANUS. Thank you very much.

Senator SPECTER. Thank you very much.

The hearing is now adjourned.

[Whereupon, at 11:20 a.m., the committee was adjourned.]

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